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Final Report

Interim Evaluation of the Financial Institutions and Expansion Project

Submitted to:

Office of Economic Growth
U.S. Agency for International Development
New Delhi, India

Submitted by:

Allan Roth & Russell Diehl
Louis Berger International, Inc.
1819 H St., N.W., Suite 900
Washington, D.C. 20006

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Final Report

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Allan R. Roth
630 Prospect Street
Maplewood, New Jersey 07040

March 31, 1997

Mr. Peter Thormann
Office of Economic Growth
U.S. Agency for International Development
B-28, Institutional Area
Qutab Hotel Road
New Delhi 110016
India

Dear Peter:

Enclosed please find Russell's and my final report of our evaluation project.

In addition to the hard copy, a computer disk is enclosed that has the final report converted into several word processing softwares. They include a DOS version (*.txt) and a Windows version of Word converted via Microsoft Office software. I work in XYWrite, and that seems to be about as anachronistic as the quill; hence, the attempt to provide the file in a more congenial form. I hope it works in one or the other of them.

Russell and I enjoyed the opportunity to work with you and Ashok. We hope our effort contributes in some measure to the further development of financial institutions in India.

Cordially,

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BACKGROUND

This is the report of an interim evaluation of the contract awarded to Price Waterhouse (PW) on November 15, 1994 to implement a portion of U.S. AID's Financial Institutions Reform and Expansion project ("FIRE project"). The goal of the FIRE project is to develop India's capital markets to mobilize and allocate capital more efficiently.

The Price Waterhouse contract is for four years. The contract provides for three categories of activities: (1) technical assistance by experts from the U.S. and India; (2) training in the U.S., and (3) training, workshops and seminars in India. The planning and monitoring system relied upon for implementing the contract is an Annual Workplan, which describes the inputs, activities and outputs that are expected for the period involved, which is normally one year. The project is in its third Workplan. The first Workplan was for the period November 1994 - April 1996; the second Workplan for November 1995 - April 1997; and the third Workplan is for November 1996 - April 1998. (A performance analysis of the FIRE project prepared by PW is included in Appendix D.)

The evaluation team was comprised of two members, who visited India in January 1997 to review the progress of the FIRE project. While in Delhi and Bombay, the evaluators met with more than 50 people, from more than 30 different organizations, who have first-hand knowledge of the FIRE project. (A list of those interviewed is attached as Appendix B.) These interviews, together with the evaluators' reviews of documents, participation in meetings with FIRE project consultants and their clients and observations of recipients of FIRE project assistance, form the basis for this report.

EXECUTIVE SUMMARY

As part of its economic reform strategy begun in 1992, India instituted a program of financial market development. The United States Agency for International Development agreed to provide a 4-year, multimillion dollar program of technical assistance known as the Financial Institutions Reform and Expansion ("F.I.R.E." or "FIRE") Project. Price Waterhouse ("PW") was selected as the contractor for the project.

The strategic objective of the technical assistance project is to reform the financial sector in order to increase the mobilization of capital. There are indications that the capital markets in India are becoming an increasingly significant mobilizer of capital. In 1996, aggregate banks deposits were Rs. 4,710 billion; the market capitalization of the Bombay Stock Exchange list was Rs. 4,323 billion. By comparison, the bank deposits in 1990 were Rs. 1,670 billion and the Bombay Stock Exchange list's market capitalization was Rs. 554 billion. Though these numbers are subject to various interpretations, it is nonetheless notable that, while aggregate bank deposits increased 182%, the market capitalization of the BSE increased 680% during the same period.

The FIRE project is designed to improve the effectiveness and efficiency of the Indian securities market by improving both the operating and regulatory environments. It has contributed significantly to market efficiency by assisting the trading markets to modernize their trading systems. In addition, a considerable advance in post-trading processes of settlement and clearing has occurred with the aid of the FIRE project.

Prior to the FIRE project, the Indian securities regulatory agency had persuaded the stock exchanges to replace their call trading systems with screen-based trading. The Indian post-trading systems, however, were still highly inefficient and ineffective, imposing high transaction costs and creating significant additional risks for share investors. As a means of reducing these investment risks and transaction costs, FIRE has provided technical assistance to improve the design and operations of a depository system set up shortly before the project began and the facilities for clearing and settlement in the secondary trading markets for securities. The technical assistance has consisted of bringing in outside experts to advise on systems and procedures and of training, both in India and abroad, of key personnel. The technical assistance and training have been demonstrably effective. (A list of the PW consultants' activities is attached as Appendix C.)

The FIRE project also has provided technical assistance addressed to improving financial market efficiency through policy and regulatory reforms. FIRE consultants have worked with the Indian securities regulatory agency, the Securities Exchange Board of India ("SEBI"), to develop regulations and codes for stock brokers, mutual funds and merchant bankers. FIRE consultants have assisted SEBI to develop courses, tests and licensing procedures to qualify stock brokers for certification.

Through FIRE's influence and technical assistance, the concept of self-regulation is gaining acceptance by securities professionals and SEBI in India. For SEBI, self-regulation is a necessary means to expand its regulatory influence beyond the direct reach of its limited staff. SEBI has required the professional intermediaries in the capital markets to organize as self-regulatory organizations (SROs), and these organizations, too, have been influenced by the FIRE project to accept the concept of self-regulation. To date, associations of brokers at the BSE and DSE have been formed. Mutual funds have organized the Association of Mutual Funds of India (AMFI) and merchant bankers have organized the Association of Merchant Bankers of India (AMBI). Through the FIRE project, visiting foreign experts have been made available for workshops, seminars, talks and individual meetings in order to explain how self-regulation works. These training and instructional efforts have succeeded in raising skill levels and heightening the awareness of policy makers and regulators of the implications of their decisions.

FIRE has successfully worked with SEBI and the stock exchanges to develop surveillance and enforcement techniques. With assistance from the FIRE project, the stock exchanges in Bombay and Delhi and the association for the mutual fund industry are committed to providing information to public investors on a consistent basis and in a form that will be useful to them.

A significant aspect of the FIRE project in furtherance of its objectives has been instructional. An interesting approach of the FIRE project has been the emphasis on involving visiting consultants in training. Consultants hold training sessions with key personnel in the organizations with which the consultants are working. In addition, training programs of various types (workshops, lectures, etc.) are regularly conducted throughout India. Key personnel from SEBI and other major capital market institutions have been sent on training programs abroad, preceded by careful FIRE project briefings and preparation. These instructional activities have produced clear results. The personnel involved testify to the importance to them of the training. The organizations for which they work have benefited from the training through improved performance at higher levels of sophistication. (Copies of illustrative reports by trainees are attached as Appendix F.)

The FIRE project has been highly successful to date, and its impact on Indian financial institution development is clear and impressive. Its technical consultants have been highly qualified, experienced in the issues faced by emerging markets, sensitive to other cultures and effective in achieving their desired goals.

There are some areas in need of greater emphasis. In the second phase of the project, FIRE should consider devoting more attention to professional development, the secondary debt market and the furtherance of SEBI's development. At this stage of their development, encouraged by FIRE's assistance and support, the clearing, settlement and depository systems have achieved sustainability. Accordingly, they would seem to be capable of funding for themselves any significant additional outside assistance they require.

I. Introduction

Background

India was jolted into a program of economic reform in 1992, and, as part of that reform program, made a commitment to develop its financial markets. The USAID Financial Institutions Reform and Expansion ("F.I.R.E.") Project was instituted to provide technical assistance on behalf of making the Indian securities market more effective and more efficient in mobilizing and allocating financial capital. While the project has three components: (i) improvement of the regulatory environment; (ii) improvement of the operating environment; and (iii) development of the debt market, the technical assistance contract with Price Waterhouse ("PW") is focused on components (i) and (ii). The contract was signed in November 1994, but, because of a dispute concerning the contract award, PW did not begin work until January 1995.

Strategic objectives

The stated strategic objective is to reform the financial sector in order to increase the mobilization of capital. The PW component is addressed to improving financial market efficiency through policy and regulatory reforms. This consists of improving securities market transparency, modernizing systems to promote the efficiency of the capital markets, reducing the current high levels of risk arising out of system inadequacies, improving the protection of investors and enhancing liquidity in the equity and debt markets.

Performance indicators

As project performance indicators, the Strategic Objective Tree sets forth a list of objective measures of capital market expansion, such as increases in the number and value of shares traded, changes in the number of issuers and investors, increases in the number of company listings, and the like. It is respectfully submitted that objective criteria do not serve as adequate measures of the effectiveness of an institution-building project of this kind.

According to the Strategic Objective Tree's objective measures, the Indian capital markets have had dramatic successes but lackluster growth. The average time of settlement, for example, has been dramatically reduced as a result of the clearing and settlement systems instituted with the assistance provided by the project.

In our judgment, an examination of the data for the capital markets does not tell very much about the effectiveness of the F.I.R.E. project. Increases in the number of new equity issues or the changes in the ratio of market capitalization of outstanding shares to GDP may or may not have any relation to the project. Increased numbers of investors may or may not indicate market vitality or the effectiveness of improved regulation or much else that would serve to measure the FIRE program's effectiveness.

A study by Professor Ajay Shah and Susan Thomas, U.S.-educated Ph.D.s at the Indira Gandhi Institute of Development Research, compares aggregate banks deposits (as a measure of banking system assets) with the Bombay Stock Exchange's market capitalization (as a measure of equity market assets) in 1990 and 1996. Whereas in 1990 the ratio of bank-intermediated assets to equity-market intermediated assets was 3:1 (Rs. 1,670 billion to Rs. 554 billion), in 1996 it was .9:1 (Rs. 4,323 billion to Rs. 4,710 billion). If corporate debt issues are added to the capital market assets in 1996, approximately 55% of the financial system's assets were intermediated through the capital markets; 45% through the banks.

Data taken from the Centre for Monitoring the Indian Economy's Monthly Review of December 1996 show the value of equity issues jumping from Rs. 181 billion in 1992-93 to Rs. 360 billion in 1994-95. Based on press reports of an independent study provided to the Ministry of Finance, however, it also appears that, as of October 1996, 72% of the share issues made during the 2-year period April 1994-March 1996 were trading below par; 44% were trading at less than Rs. 5. Another study of 240 companies that went public between April 1996 and July 1996 showed that 28 of them were under subscribed.

Project focus as it has evolved

Market efficiency implies that funds flow on the basis of informed evaluations of risk and potential return. Transaction costs are a function of market efficiency. In the Indian market, the clearing and settlement "costs" are major elements of transaction cost because of processing delays, fraud and counter party risk.

After a systematic assessment of the specific needs to be addressed, PW's assistance has devolved into seven project focuses:

1. To reduce investment risk by shortening clearing and settlement time for secondary market trades in both stocks and bonds.

2. To transform the stock exchanges and associations of various securities market intermediaries into self-regulatory organizations.

3. To develop a functioning secondary debt market in India.

4. To improve the effectiveness of the regulation India's securities markets toward the objective of reaching international standards.

5. To develop risk management and increase liquidity.

6. To assist in the development of India's mutual fund industry in order to broaden India's retail investor base and mobilize additional resources through the stock and bond markets.

7. To institutionalize capital market training and research.

Project methodology

PW has annual work plans that are approved by USAID. The plans are also approved, or developed in consultation with, SEBI.

A resident chief of project is in Bombay. Individual consultants and specialists are brought to India as needed for specific purposes pursuant to task orders. To date, there have been at least 25 task orders.

PW began by examining the general level of sophistication of the market participants through a survey of 127 people working in the stock exchanges, SEBI, SCHIL, the Credit Rating Information Services of India, brokers/other market intermediaries and financial training institutions. The survey enabled PW to identify, by subject area, where training is most needed and where the greatest gaps in understanding were. On this basis, PW set its priorities for training and education.

II. To Reduce Investment Risk by Shortening Clearing and Settlement Time for Secondary Market Trades in Both Stocks and Bonds.

The goal of this project focus is to upgrade and modernize the system for trading securities and the post-trading systems. In recognition of the high transaction costs resulting from a highly inefficient and expensive process of trading securities and of clearing and settling trades on the stock market, SEBI has encouraged the establishment of screen-based trading as a replacement for the traditional call system previously employed.

Background

The National Stock Exchange (NSE), organized as a competitor to the traditional, and member-dominated, Bombay Stock Exchange (BSE), began operating in April 1994 as an automated exchange. At the outset, the NSE committed itself to modernize the clearing and settlement process in India and, for this purpose, established the National Securities Clearing Corporation, Ltd., ("NS Clearing") as a wholly owned subsidiary. NS Clearing was incorporated in August 1995 and began operations in April 1996.

Originally, the Stock Holding Corporation of India, Ltd. (SHCIL) was organized to handle clearing and settlement and to serve as a securities depository. In May 1995, PW began work with SHCIL on a National Clearing and Depository System, preparing a set of specifications to use as a basis for inviting bids from outside vendors of systems for the clearance and depository operations. In July 1995, PW submitted a set of requirements for this purpose and thereafter assisted SHCIL in evaluating the proposals submitted by the outside vendors who responded. Subsequently, SHCIL's credibility was impaired by unrelated problems, and it was decided to organize a new and distinct depository organization.

The National Securities Depository Limited (NS Depository) was created in February 1996 to take over the depository activities from SHCIL. PW was requested to prepare an organizational plan for the NS Depository, which it submitted in July 1996.

With NSE as a model, in December 1995, SEBI met with the stock exchanges to set forth a program of reform that required the exchanges to adopt screen-based trading systems, to simplify share transfer procedures, to reduce settlement cycles, to develop stock-watch programs and to incorporate transparency obligations into listing requirements.

What has FIRE done?

The July 1995 work with SHCIL on a National Clearing and Depository System produced a primer on clearing/settlement and depository operations that has provided a blueprint for the NS Depository and the NSE. There are two elements to the FIRE work: development of the trading system and post-trading systems development.

Trading system development

FIRE has assisted NSE, and to a lesser extent other exchanges, with trading system development. Specifically, FIRE assisted:

- NSE and the Over the Counter Exchange of India (OTCEI) with their development of screen-based trading systems,
- NSE with its organizational structure,
- NSE and OTCEI with their back office systems, including data security and business interruption procedures;
- the Bombay Stock Exchange (BSE) and the Delhi Stock Exchange (DSE) with cost studies of clearing/settlement and depositories, and
- the regional exchanges by working with them to decide whether, and if so, how, to interconnect.

Post-trading systems

In connection with post-trading systems, FIRE has assisted with the NSE's and OTCEI's clearing and settlement systems and with the NS Depository (NSDL). In addition, PW prepared cost studies of post-trading systems for BSE and DSE. As a result of the DSE study, DSE decided not to create its own depository. Although subject to further review, BSE remains committed to creating its own depository.

To assist with the modernization of the post-trading systems development, in November 1995, a PW consultant worked with NSE on back office systems. Shortly prior to that, another PW consultant worked with NSE to develop systems for data security and business continuity. In May 1996, FIRE did a technical evaluation report on the NSDL depository system. In July 1996, a PW consultant developed an organizational structure plan for NSDL, followed by a workshop for the management of NSE assigned responsibility for getting the NSDL into operation.

In April 1996, a FIRE consultant addressed the issue of information systems risk at the OTCEI. This was a review of the data base management and physical/data security issues related to the use of computers for processing trades, settlement and back office operations. The consultant, in addition to making suggestions regarding security policies, data centers, business continuity planning and control/security for the depository, proposed a separate clearing corporation for OTCEI and putting new types of financial instruments into the automated systems.

What impact has the FIRE assistance had?

Trading of shares in India is now conducted through an automated system available throughout the country. Pricing is more transparent than ever before, with bid and offer prices and reports of last sales available on a real-time basis on computer screens in brokers' offices. On the NSE, clearing and settlement is handled by a separate clearing subsidiary, using automated systems. The clearing and settlement cycle has been reduced from 14 days to 7 days.

NSE now accounts for about 60% of the total volume of trading in the secondary market and has succeeded in stimulating the other stock exchanges to adopt the modern techniques for trading and to overcome their inertia regarding improved clearing and settlement. BSE is about 30-35% of trading, and it has had to accelerate its schedule for modernizing in the light of the competitive pressures from NSE. BSE, too, has shortened its clearing and settlement cycle to 7 days, but brokers employ a system, called "bodla" to engage in a form of forward-market activity that distorts measures of clearing and delivery cycles on that exchange.

OTCEI has about 5-10% of the trading activity, and it is searching for a market niche. While the OTCEI has been a spur for reform along with NSE, its role has been to serve as the marketplace for small capitalized companies. This does not fully utilize the OTCEI's modern systems and capacity.

OTCEI also has a separate clearing subsidiary, also using automated systems, and their trades settle 5 days after taking place, with payment made 7 days from the date of the trade. This is on a rolling basis; that is, instead of having one day designated as the settlement day for all trades occurring within the previous cycle, trades are settled on a continuous basis, with the settlement taking place 5/7 days after the trade is made.

NSE has the capacity to monitor the credit status of its trading members on a real-time basis and to disconnect from the trading system any trader who has exceeded permissible credit limits. This is a major innovation in India.

The first trades of securities lodged in the depository and therefore not requiring physical transfers of paper were completed in late December 1996. While only a handful of share issues are presently in the depository system, those shares which are in the system trade at a 3% premium over shares that require physical transfer and delivery.

Conclusions and recommendations

At this stage, the depository and clearing/settlement systems are developed and operating. While they undoubtedly can always use more technical help, the FIRE project resources would be better applied toward assisting in areas of greater need, such as the development of the legal infrastructure or the accounting profession. SEBI, and to a lesser exchange, the stock exchanges, are committed to the concept of clearing/settlement and depository systems. There is no reason to expect these institutions to be abandoned if FIRE ceases to provide support. Accordingly, any future assistance they may need should come from local resources, including the institutions that benefit from them.

The value of more than one depository for India is questionable. With the available technology, the site of the depository in relation to the stock exchange is not a factor; it is feasible to have one depository for all India. The Bombay Stock Exchange should be encouraged to abandon its refusal to join the existing depository, the NSDL. The Dehli Stock Exchange is on the verge of joining the NSDL and should be encouraged to take the final step.

III. To Transform the Stock Exchanges and Associations of Various Securities Market Intermediaries into Self-regulatory Organizations.

A significant aspect of the FIRE project effort in furtherance of this project objective has been educational. The concept of self regulation is uniquely a product of the U.S. legal environment, and it has had to be "transplanted" to India. As a result, it needed to take root, and that has what PW has been trying to achieve.

SEBI has accepted the concept of self-regulation as necessary to enable them to expand their regulatory influence beyond the direct reach of their limited staff. SEBI has required the professional intermediaries in the capital markets to organize as self-regulatory organizations (SROs). To date, associations of brokers at the BSE and DSE have been formed. Mutual funds have organized the Association of Mutual Funds of India (AMFI) and merchant bankers have organized the Association of Merchant Bankers of India (AMBI). AMBI, however, is not yet committed to accepting a role as a self-regulatory organization. The merchant bankers in India are divided in their views on the value of AMBI's being a self-regulatory agency.

What has FIRE done?

PW has assisted SEBI, NSE, BSE and the associations of merchant bankers and of mutual funds to understand the concept of self-regulation and the role of self-regulatory organizations. The assistance has taken the form of one-on-one discussions with leaders of these institutions, training programs in the U.S. and public educational programs in India. Typical of the latter was the third conference on mutual funds held in January 1997, where Mr. David Silver, former head of the Investment Company Institute in the U.S., was a keynote speaker and available for several days for informal talks with mutual fund industry leaders in Delhi and Bombay.

As a first step toward professionalizing stock brokers, PW has worked with SEBI to design and implement a broker testing, certification and licensing program. In October 1995, SEBI initiated the formation of a committee to set standards of persons acting in the capital market, especially brokers and sub-brokers. Beginning in November 1995, a PW consultant worked with this committee. A draft of a test for this purpose was developed by the Unit Trust of India Capital Markets Institute and the Institute of Chartered Financial Analysts. The PW consultant returned to India to assist with the preparation of the final draft of the test and for additional work on the certification and licensing matters. In May 1996, the PW consultant drafted a "consultative paper" to explain the committee decisions and reasoning for the interested public. At the same time, the consultant drafted a syllabus for a training program for the test. In January 1997, SEBI released a "consultative paper" inviting comment and discussion on proposals for testing, certification and licensing which follows very closely the consultative paper prepared by the FIRE consultant.

A nettlesome issue related to self-regulation by the appropriate professionals in the market is how to bring the sub-brokers into the system. Sub-brokers form an extensive network linking the stock exchange brokers with the retail investors and linking diverse regions of the country. The law under which SEBI operates literally calls for the registration of sub-brokers, as well as brokers, but SEBI has been overwhelmed in its attempts to implement that provision. As a result, the registration of sub-brokers is in a state of limbo. The issue of setting qualification standards for sub-brokers is even more difficult, and SEBI has not yet addressed that issue. In an effort to sort these matters out, a committee has been created, and a PW consultant has been working with this committee.

As early as October 1995, a PW consultant reviewed the rules and regulations of the National Stock Exchange of India, Ltd. and its status as a self-regulatory organization. Since NSE is not a member-owned stock exchange, it is unique among exchanges in its governance structure and its relationships with the trading brokers. Its board of directors is comprised entirely of representatives of NSE promoters, professional employees and outside legal counsel. The promoters are GOI financial institutions. In this sense, it is different from other self-regulatory organizations.

In September 1996, a PW consultant worked with AMFI to develop a comprehensive strategic plan for its development as a self-regulatory organization. This work is described more fully in the section that discusses the mutual funds (section 7, below). FIRE has followed this up with a subsequent visit by the same consultant to work with AMFI on the implementation of that strategic plan. A national conference of mutual funds, including the visit by David Silver mentioned above, was a part of that effort.

With respect to the merchant banking community, the picture is somewhat different. Prior to the requirements of law for merchant banks to register and qualify with SEBI, the merchant banking community in India comprised about 40-50 firms. Representatives of this group with whom we met claim that the limited group exerted sufficient peer pressure on each other that assured competence and accountability. If so, this would be similar to the system in Great Britain before the "Big Bang". With the new securities law, as implemented by SEBI, the merchant banking community now is comprised of about 1,000 registered firms. Accordingly, the peer pressures of the old "club-like" group are no longer adequate to the needs, and SEBI has required the formation of a self-regulatory organization.

PW does not appear to have had any formal projects addressed to improving the self-regulatory capabilities of AMBI. In its third work plan, PW proposes to institute projects for assisting SEBI to draft rules governing the SROs, specifically naming OTCEI, AMFI, NSDL "and other exchanges and market participants". Specifically not mentioned is AMBI.

What impact has the FIRE assistance had?

As discussed more fully in connection with the discussion of mutual funds, below, AMFI shows signs that the self-regulatory concept has taken root. The emphasis of the FIRE project now is to encourage AMFI to be more active, and more public, in the enforcement of its rules and standards.

In a front page article in The Financial Express on January 22, 1997, Pratip Kar, the SEBI executive director with responsibility for mutual funds, publicly rejected AMFI's request that SEBI relent from its position of imposing added responsibility on mutual fund asset managers and trustees. In our view, this publicizing of a rejection of AMFI's importuning on behalf of the AMFI membership strengthens AMFI by demonstrating to its membership that SEBI is AMFI's overseer. The message to the AMFI members is that there is no escape from accountability to a regulatory agency. The choice for the members then becomes whether to come to terms with AMFI as their regulator or face direct regulation by SEBI.

In discussions with representatives of NSE, BSE and OTCEI, the senior managers evidence a clear understanding of the need for their organizations to become effective SROs. In newspaper articles, the BSE is reported to be conducting high-profile investigations of market rigging and other improper conduct, the NSE announces that two of its members have been declared to be in default for failure to meet delivery and the Delhi Stock Exchange is reported to be investigating what happened to a company that recently listed but then disappeared from view.

Perhaps evidence of the successful rooting of the concept of self-regulation comes from the negative implications to be derived from the comments of a columnist in the Dalal Street Investment Journal, January 5, 1997, entitled "SEBI's Follies" (p. 116), where the author bemoans that "...SEBI is only here to act as a watchdog . . . . It is time SEBI takes an initiative for the revival of the markets, which are in the doldrums. . . "

Conclusions and recommendations

The FIRE project has done a good job of getting SEBI and the financial community to accept the concept of self-regulation. This is an important contribution of the FIRE project, and it requires continued effort. Self-regulation is a concept of the common law systems, and it is a difficult concept to transplant to another culture.

While the FIRE project appears to have succeeded in getting SEBI and Association of Mutual Funds to accept the concept and to agree to put it into practice, continued assistance is needed. Both SEBI and AMFI need more technical assistance and training to help them continue the work they have begun in this area; other SROs need to be encouraged to implement effective self-regulatory programs. SEBI needs to continue to develop its staff, both in size and expertise. The FIRE project should assist with the training of new staff in operating in a self-regulatory system and with the drafting of appropriate SEBI rules for oversight of the SROs.

AMFI is only at the beginning stages of developing into a self-regulatory organization. It would be prudent to continue to work with AMFI until it is clear that they are able to continue unaided without regressing.

The merchant bank members of India do not appear to have accepted the concept of self-regulation and of AMBI's role as a self-regulatory agency. FIRE would need to devote more energy and provide more assistance merely to persuade the merchant bankers to agree to make AMBI into an effective self-regulatory agency. In our judgment, some form of self-regulation by merchant/investment bankers is critically important. The FIRE project should consider alternatives to the model developed for AMBI in the event that AMBI does not succeed in becoming an SRO. For example, merchant bankers might be classified as brokers/dealers and required to become members of a stock exchange or to join a self-regulatory organization of brokers, thereby coming within the ambit of a self-regulatory structure alternative to AMBI.

IV. To Develop a Functioning Secondary Debt Market in India

In contrast to the accelerated growth of the equity markets in India beginning in the 1980s, India's debt market has developed slowly. It has not yet become a significant source of finance for the private corporate sector. Historically, the debt market has been driven by public sector requirements. The statutory liquidity requirements of the Reserve Bank of India (RBI) requires Indian banks to invest a specific percentage of their liabilities in government-designated instruments. This system has virtually transformed India's debt market into a captive market for government finance. The forced purchase of government paper uses a considerable amount of banking sector assets and crowds out the country's private sector. While progress is slow, the statutory liquidity requirement is being phased down, and some government debt is subjected to auction.

The debt securities market in India is estimated to be around US $40 billion just for the government sector. These debt securities are bought at issue by a variety of financial institutions (e.g, commercial banks, insurance companies, provident/pension funds and diverse non-bank financial institutions) in order to meet statutory requirements of different sorts. As a result, even though the primary market is large, it is also captive, and there is not an active secondary market to meet liquidity needs.

Public sector corporate entities have about US $10 billion outstanding. These bonds carry interest rates ranging between 10% - 14%. Most of these bonds appear to be placed with banks, mutual funds and large non-bank financial institutions.

Private corporate entities issue bonds with market-driven rates ranging between 16% - 19%. Placed privately with financial institutions, these securities are not actively traded, even though by law, they are rated and listed on the stock exchanges.

The key factor influencing the demand for debt financing has been the prevailing rate of interest. Interest rates in India traditionally have been administered to a high degree. Though there has been some freeing of rates, they are still dominated as a result of the statutory requirements, which render the rates not market driven. The combination of this government influence over the interest rate and various regulatory constraints, such as restrictions on repurchase agreements, a variety of local stamp taxes, a bar on short-selling, lack of an interbank rate and the like, have impeded the development of portfolio management of debt instruments. That, in turn, forestalls trading and a secondary debt market. Until market-driven rates are adopted for government debt, there will not be the essential reference rate upon which to set the prices of other debt instruments.

What has FIRE done?

In January 1996, a PW consultant conducted a thorough study of the Indian debt market. The following recommendations were made in a report entitled, "Review of the Operational Impediments of the Debt Market in India":

- allow primary dealers to underwrite debt securities
- allow repurchase agreements
- SEBI guidelines for public issues to allow less than 90% subscribed debt issues to be successfully underwritten
- credit agencies, together with SEBI, should require more detailed financial history and projections from companies
- accounting standards should be developed and companies required to follow them
- implement depository
- primary dealers should form an inter-dealer network
- change method of calculating primary dealers' current account status with RBI
- change newspaper reporting to trade date from settlement date
- fully automate clearing and settlement
- include debt instruments in central depository
- explore ways to expand range of securitized debt instruments
- allow short selling of bonds
- RBI should develop bank reference rate
- absent a benchmark, develop a bond index
- portfolio managers should mark to the market periodically
- eliminate or standardize taxes on debt instruments
- pursue a recommended research and dissemination strategy
- provide extensive participant training and local training

The first and second annual PW work plans did not include debt market projects in their technical modules. The third annual work plan does provide for several debt market consulting activities. Principal among these is active promotion of a bond dealers association as a self-regulatory organization. This is expected to take place in two phases: First, the formation of debt market committee to formulate policy and conduct research related to formation of an SRO. Second, the formation of the SRO, the framing of appropriate rules and the planning required to implement them. The projected technical assistance recognizes that changes will be required in existing regulations.

The third Workplan also contemplates linking the debt market with the improved clearing and settlement systems used in the equity markets. It is contemplated that this will be helpful in promoting the development of the secondary debt market.

Training in the form of a series of five workshops on the management, marketing and trading of debt instruments is planned during the period of the third Workplan (November 1996 - April 1998).

What impact has the FIRE assistance had?

The FIRE project director, in an interview published in The Business Standard on September 20, 1996, calls for the development of a "bigger debt market", especially if India is to meet its infrastructure financing aspirations. To date, FIRE has provided a first-rate study on the debt market. It is our understanding that the seminar for NSE and the debt market workshop that were anticipated to follow the study were not conducted, however.

The role of a market-driven pricing system for debt instruments and the importance of a secondary market are by now acknowledged. A useful treatment of the subject, authored by Sid Kapur, appeared in The Business Standard on January 16, 1997, and a copy is attached.

Conclusions and recommendations

There is a semblance of a money market in India, and some range of government financial instruments already is available. As a result, there may be a basis on which to build a secondary debt market in India.

The importance and value of a debt market are generally understood and appreciated, but neither India's policy makers nor the FIRE project has made the commitment necessary to its development. The debt market establishes benchmarks for interest rates and rates of return in the financial system. A viable secondary debt market would mean that debt instruments would be liquid and therefore usable financial assets for a broad array of financial managers and financial institutions. The added choice of financial assets would enhance financial management by affording more opportunities to diversify risk. If debt instruments become viable forms of financial assets, i.e., liquid and tradeable, there could be more variety of financing techniques. Various assets could be "securitized" enhancing the liquidity of those assets.

The FIRE project study of the debt market produced a report identifying the critical issues and recommending the initial action required. More should be done to follow up on the recommendations made in that report. If the FIRE project were to give more emphasis to bond market development, it may be possible to persuade the Government, at least, to address the impediments to secondary market activity created by restrictions on repurchase agreements, local stamp taxes, the prohibition of short-selling and the lack of an interbank rate. In addition, the FIRE project might lend its voice to those of others advocating market-driven rates for government debt.

After this review was conducted, but before the submission of this report, the GOI announced its budget plan. The plan proposes steps to improve the climate for the development of the secondary debt market. The GOI commitment to secondary debt market development provides a propitious time for the FIRE project to intensify its efforts in this area.

V. To Improve India's Securities Markets Regulations, Monitoring and Enforcement to International Standards to Enhance Transparency and Investor Confidence.

FIRE has set out to achieve this project objective by providing assistance (a) to SEBI to develop regulations and codes for various market participants and an effective enforcement and inspection plan; (b) to stock exchanges to develop effective surveillance and enforcement techniques; and (c) to implement investor information centers at both SEBI and stock exchange levels that will provide investors access to financial and other material information about the issuers on a periodic basis.

In 1995, with enactment of a new ordinance, SEBI was granted important authority to intensify its market supervision activities and to impose sanctions for violations of law.

What has FIRE done?

With respect to SEBI, PW has assisted to develop its enforcement capability by guiding SEBI to understand the importance of enforcement and by assisting SEBI with the organization of its enforcement activities. In November 1995, Cliff Kennedy, formerly of the U.S. SEC, reviewed SEBI's enforcement plan and recommended "thrust areas" for SEBI improvement. While in India, Mr. Kennedy also presented a workshop on securities market enforcement issues and techniques. This is part of the broad effort to assist SEBI in improving its surveillance and compliance capabilities.

Mr. Kennedy reviewed a broad range of issues involved in SEBI's enforcement program, including (i) authority granted SEBI under SEBI Act; (ii) SEBI regulations on insider trading, market manipulation and other violations; (iii) inspections and enforcement activity. He also reviewed how well SEBI was functioning as an enforcement authority and developer of SROs. He found that, on the whole, there was little effective enforcement of applicable laws and regulations in the Indian securities markets and that SEBI had to play a greater role in enforcing its rules and regulations.

This was followed up in January 1996, when Terry O'Malley, a former SEC enforcement staff member, worked with SEBI on further development of its enforcement program. Training for SEBI's enforcement staff followed. Seminars have been conducted for SEBI enforcement staff and for BSE and NSE staff. SEBI Chairman Mehta visited the U.S. in 1996 under FIRE sponsorship. This visit encouraged him to push for a stock watch program in India. PW plans to work with SEBI and the exchanges to institute stock watch programs. This will include workshops and seminars for personnel to be involved in the program.

SEBI's enforcement activities, of course, are relevant to the stock exchanges, the merchant banks and the mutual funds, as well as the stock brokers. The PW consultants found that SEBI needed to strengthen professional organizations as self-regulatory organizations so that SEBI's limited resources could be leveraged. FIRE recommended that SEBI draft legislation to strengthen the penalty provisions of the applicable securities laws. Finally, the PW consultant found that SEBI needed to enlarge and strengthen its enforcement staff.

In the case of the stock exchanges, FIRE has furnished a consultant to the NSE to review that exchange's rules/regulations and its capacity for enforcing them effectively. The stock watch programs that SEBI wants the exchanges to institute, noted above under the discussion of self-regulation, are in the process of evolution, and PW consultants have been assisting NSE and OTCEI with this. BSE claims also to be working on a stock watch program.

What impact has the FIRE assistance had?

FIRE has provided needed training and skill development for the SEBI enforcement staff. Interviews with program participants discloses that the training has been effective in providing both a broad and a specific understanding of SEBI's regulatory role and its importance to the development of the capital markets. Senior members of the SEBI staff, including the chairman, were provided access to counterpart organizations in the U.S. and other countries that have proven invaluable to them. They freely admit that without the FIRE program, they would not have such access, and they confirm that the access has been important to them in the performance of their jobs.

Managers and staff from other capital market organizations who participated in FIRE sponsored training programs similarly volunteer that FIRE provided them with a window on relevant practices and experience in other countries. The awareness of other practices has made them more conscious of the critical elements of Indian practice and, therefore, better able to think independently about how best to function in India.

BSE, NSE, Delhi Stock Exchange and OTCEI have all taken action to increase investor awareness through investor oriented programs and publications of the exchanges. Here too, the influence of FIRE training programs and participant training opportunities is evident.

Conclusions and recommendations

The technical assistance and training efforts in this area are continuing, and they should. The project objectives are important to capital market development, and the continuation of assistance is warranted.

- The projects are well focused, and they have been effective;
- The technical assistance and training programs have been well designed;
- The cooperation of SEBI and the stock exchanges has been good;
- There are clear signs of results;

In our judgment, the FIRE project has been highly successful in pursuit of this project objective. In the time remaining on the project, and if extended, in the succeeding project, other issues that need to be addressed with respect to reaching international standards include more emphasis on issuer disclosure and the development of other critical professionals.

The FIRE project should pay more attention to issuer disclosure. If the internationalization of the Indian market includes attracting foreign investors to Indian company securities, those companies must meet the transparency expectations of international investors. Even if the concern is not with attracting foreign investors, the companies need to operate with greater openness to domestic public investors. Company managers need more training related to issuer disclosure. The pressures from the financial markets are a strong inducement to corporate efficiency. The FIRE project could assist this development through public seminars and workshops for corporate managers and other interested parties.

The accounting and legal professions also have a pivotal role in the corporate and financial systems. The existing local capacity to provide training in the workings of the financial system for lawyers and accountants is inadequate for the level of sophistication needed. The FIRE project could play an influential role in raising the levels of sophistication of these professionals by assisting in the establishment of training facilities and the design of training programs. A similar need arises with respect to skilled securities analysts.

SEBI's participation in the professional development and training of analysts, accountants and lawyers should be encouraged for several reasons: First, the give-and-take of such programs would help to develop understanding and rapport between SEBI and the professionals upon whom they must inevitably rely for the regulatory system to work. Second, SEBI's involvement would encourage participation by enhancing the perception of authenticity and immediate professional applicable value of the programs.

The relative responsibilities for disclosure review of SEBI and of the merchant bankers underwriting an issue need to be worked out. AMBI is not presently capable of functioning as an effective self-regulatory organization to set and enforce standards for merchant bank due diligence obligations. Either SEBI should impose the obligations on merchant bankers by rule or SEBI should review prospectuses. In both cases, SEBI will require assistance from the FIRE project to build the staff skills needed.

The FIRE project should consider increasing its technical assistance addressed to training securities analysts for the SEBI staff and by assisting in the formulation of the specific disclosure requirements imposed by SEBI. There is little doubt that both SEBI and the FIRE project recognize the importance of issuer disclosure to the financial markets and to corporate efficiency. The risk is that the project will end before this issue gets the attention it deserves.

VI. To Develop Risk Management and Increase Liquidity

PW has undertaken to achieve this goal by providing assistance:

(a) to SEBI to develop a regulatory framework for futures and options markets; and
(b) to NE to establish a futures and options exchange.

What has FIRE done?

At the request of NSE, PW retained a consultant to conduct a study of the feasibility of establishing a derivatives market in India. The study was concluded in March 1996. The study concluded that India is not yet ready for a derivatives market institutional shortcomings and inadequate technical capabilities. Among the institutional shortcomings that preclude futures and options trading at this time are the absence of short-selling and the lack of facilities to enable short-selling (e.g., capacity to borrow securities, to borrow freely against securities, to depend on delivery of shares in transferable form) and uncertainty that the laws are adequate to the needs. In all, the study report listed 15 specific impediments.

In addition to the institutional shortcomings, the consultant identified certain technical capabilities as necessary for an equities derivative market. These are scripless trading, a securities depository to immobilize securities and the capability to transfer funds on a T + 1 time frame.

In early 1997, FIRE retained consultants to review again the feasibility of instituting trading in futures, options or indices. Additional consultancies are scheduled for March and April 1997. Scheduled to coincide with each of these visits are two-day workshops and seminars, with an estimated attendance of 225 market participants.

SEBI has a derivatives committee established to consider whether or not to establish a derivatives market, and, if so, how. PW is working with that committee.

In the third Workplan, PW proposes to design educational materials for NSE to use in preparing public receptivity for derivatives market. PW also will provide materials on broker licensing, testing and certification for selling derivatives. It is planned to prepare a risk disclosure document that investors will have to execute to indicate awareness of risks. Training for SEBI, NSE, and BSE staff in market regulation and oversight for a derivatives market is also projected.

What impact has the FIRE assistance had?

Derivative securities and the markets for trading them allow market participants to manage their risks more effectively, basically by hedging. Before markets in derivative instruments may be introduced, however, the underlying cash markets will have to become more liquid. FIRE's assistance to the automation of clearing and settlement and to the implementation of the depository system contribute to making the cash markets more liquid, but there is still a great deal more needed. The stock exchanges will need to develop their basic infrastructures and information systems more fully than they have to date to reach the market discipline that derivative trading requires. In addition, the appropriate instruments must be chosen with great care, and the procedures for derivative trading fully developed. It is likely that legislation will be required to make suitable changes in relevant laws so that qualified institutions may use and trade derivatives.

The issue that needs additional consideration is whether India needs derivatives at this time. The importance of derivatives is to enable investors to reduce risks in managing their portfolios, but how widespread is the need to reduce risks in this way? For whom is this form of risk reduction important? The most active derivative markets, where derivative markets exist, are in T-bills to control interest rate risk, in foreign exchange to manage currency risk, in market indices to cope with stock market fluctuations in the management of large portfolios of equities.

In India, there are no derivatives based on interest rates or foreign exchange derivatives based on the Rupee. Before these derivatives can develop, government action will be required. Accordingly, if there is to be a derivative market in India at this time, it would have to be based on the equity market. If so, the most logical candidate for a derivative is a stock index.

Professor Ajay Shah of the Indira Gandhi Institute of Development Research has been conducting research in this area and has published some thoughtful papers. Professor Shah is an advocate for derivatives trading, and in a chapter of his forthcoming book, India Development Report, to be published in January 1997 by Oxford University Press, Professor Shah makes the following case for an index derivative:

> For a variety of strong reasons rooted in economic theory, index derivatives are uniquely placed to acquire extremely high levels of liquidity (i.e., low impact cost) as compared with derivative contracts based on individual securities. Index derivatives also fit into the indexation industry, and satisfy a much-felt need to trade the entire index as a portfolio. Modern portfolio theory holds that the fluctuations in returns on every well-diversified portfolio are dominated by the fluctuations of the market index - this makes hedging strategies based on the market index very important for anyone who owns a well-diversified portfolio. Finally, index derivatives will improve the degree of market efficiency of the market index as a whole. [Emphasis in original] Today, trading the entire index (when speculation on the index)faces the high transactions costs of buying or selling the entire index portfolio. With index derivatives, the transactions costs faced in index speculation will shrink, and hence the quality of market efficiency on the market index will improve.

The issue remains, however, whether the institutional prerequisites for any derivative market are likely to be in place in India any time soon.

Conclusions and recommendations

The FIRE project is just getting started in its consideration of derivative markets in India. PW has correctly concluded that it is premature to introduce derivatives at this time. Much of the infrastructure needed for futures, options or other derivatives is lacking. The systems for the transfer and delivery of securities, for example, are still inadequate to support such markets, notwithstanding the advances made to date.

At the same time, a lot of helpful groundwork can be undertaken by the FIRE project. Futures and options are highly correlated to other issues connected to risk management, such as brokers' capitalization, brokerage accounting practices, clearing and settlement and the system of Bodla. PW should consider recommending to SEBI that an outside study be commissioned of the Bodla practice. Bodla seems to be a key to how the BSE really works; yet it is not fully understood. A study of the practice and its implications would be useful for policy makers and others to understand what is at issue. It may bring to light practices and issues relevant to policy regarding derivatives, options, futures, etc.

To the extent the objective is to satisfy the needs of portfolio managers and others for enhanced liquidity, there may be other means for meeting the objective, such as development of a viable debt market, discussed above, that are more readily attainable. Clearly, however, there is strong pressure for some form of derivatives, and the FIRE project should be prepared to assist with the development so that it occurs sensibly. Accordingly, the area must continue to be a focus of the FIRE project.

VII. To Develop India's Mutual Fund Industry

The objective of this project focus is to broaden India's retail investor base and mobilize additional resources through the stock and bond markets.

What has FIRE done?

Poor performance and scandals had seriously damaged the standing of the mutual fund industry in India. AMFI was incorporated in August 1995 and, in July 1996 requested FIRE help to develop a promotional campaign for the industry. FIRE persuaded AMFI of the need to undertake a broader effort, to begin by gathering information related to mutual fund operations in India, investor attitudes and SEBI activities related to mutual funds. PW then recommended a comprehensive strategic plan to AMFI and persuaded AMFI that, more than a promotional campaign, AMFI needs a professional code of conduct and effective oversight and enforcement of the mutual funds.

On what appears to be a separate track, SEBI has a mutual funds division which prepared a Mutual Fund 2000 projection for the industry's development in India, and it requested FIRE assistance for specific activities identified in that projection. The specific activities for which assistance has been sought are in answering the following questions: What should the structure of mutual funds be in India? What regulations are needed? How should SEBI handle mutual fund registration? What should be the governance structure of mutual funds? How can the industry trade/self regulatory organization be strengthened?

In September 1996, a PW consultant assisted AMFI to develop a comprehensive strategic plan. The plan includes:

- a statement of principles, including acknowledgment that AMFI is dedicated to defining and maintaining "high ethical, commercial and professional standards"
- a code of conduct
- a model operations and compliance manual for Asset Management Companies (AMC)
- a commitment for AMFI to be an effective self-regulatory organization
- a draft set of rules
- disciplinary procedures, and
- a commitment to monitor compliance.

In January 1997, the PW consultant returned to India to work with AMFI on the implementation of the strategic plan. A conference of mutual funds was held at which AMFI's role as a self-regulatory organization was explained and promoted. The PW consultant worked closely with AMFI to develop the program and to conduct it.

In addition to working with AMFI, the FIRE consultant has worked with SEBI on the adoption of appropriate rules and regulations related to the mutual fund industry. FIRE has emphasized the importance of active enforcement activity by AMFI and has attempted to get AMFI to take dramatic action that would establish it as an effective enforcement agency. From discussions at which we were participants, it appears that AMFI understands the importance of this, but it has not yet taken any specific action that would achieve the objective.

In connection with the development of adequate supervision and enforcement, FIRE is also assisting SEBI to formulate appropriate regulations for mutual funds.

What impact has the FIRE assistance had?

As of July 25, 1996, AMFI had 22 members. AMFI is the most developed of the self-regulatory associations. It has progressed in developing its code of conduct and professional standards, its member mutual funds are actively involved in the association and it conducts an active program for its members and for the public.

A publicized policy dispute between asset management companies and trustees on one side and SEBI on the other concerning the scope of the responsibility of these organizations is evidence of the active role that SEBI has come to play in connection with mutual funds.

The FIRE consultant is now attempting to get AMFI to undertake a highly visible enforcement action to demonstrate that it is an effective overseer of its members conduct.

Conclusions and recommendations

In this area, the FIRE project appears to be on target: It has a clear set of goals and objectives. An action program is in place and is being actively pursued. And it is evident that the assistance being provided by the FIRE project is effective and producing progress.

At the same time, the mutual fund industry in India has serious problems. Some funds have made unreasonable commitments to investors, and the costs of keeping those commitments are now starting to be paid. Because of the thinness of the secondary market, mutual fund portfolios cannot be adequately balanced. The limited tools available to portfolio managers restrict those managers in ways that impede mutual funds in serving the investor needs for which they are most suitable: pooled investment under professional management and diversified risk.

The FIRE project has just begun to make headway in this area, however, and continued assistance is required. PW will need to work with AMFI, SEBI and the other concerned market institutions at least for another year or two.

Because of the limitations of the Indian financial markets and the limited array of financial assets available to them, fund managers lack experience with diverse forms of financial assets and markets that offer a wide array of choices. Under existing conditions, there is little room for innovative portfolio management techniques and practices. If there were the opportunity for such techniques and practices, however, it is not clear that there are many managers with the skills to innovate. The capacity is there; it needs to be developed.

VIII. To Institutionalize Capital Market Training and Research

PW has committed itself to address this project focus by providing assistance (a) to local human resource development institutions to train the future market professionals; and (b) to local research organizations to carry out quality research on various capital market topics.

What has FIRE done?

In June, 1995, at the outset of the FIRE project, PW retained a consultant to conduct a training needs assessment based on in-country visits and questionnaire polling during the period March - June 1995. The consultant conducted a survey of selected groups to determine their level of knowledge and skill about capital markets. Those surveyed were: SEBI, NSE, BSE, OTCEI, SCHIL, DSE, Training and Research Institute of BSE, DSP Financial Consultants, JM Financial & Investment Consultancy Services, Credit Rating Information Services of India, Ltd., UTI Institute of Capital Markets.

The survey identified subject areas where training is most needed and the priorities that should be attached. In a Training Needs Assessment Report in June 1995, the strategy for capital market training proposed was to:

1. to strengthen the abilities of the core group of financial managers to develop the Indian capital market to meet internationally acceptable standards of regulation, operations and investor protection.
2. to institutionalize training programs so that they become a regular part of the financial management curriculum in Indian educational and training organizations.

A summary of the completed training activities of the FIRE project is provided in Appendix E.

What impact has the FIRE assistance had?

The strengthening of the core group of financial managers has been through in-country training sessions of various types and foreign training trips, especially to the U.S. PW has managed the foreign participant training in 2 key ways: managed the participants' expectations before they went; managed the program at the point of delivery in the U.S. The Baruch program is illustrative of the project's approach. Before the participants departed India, PW's training specialist made sure that the participants knew what to expect. The training specialist personally was in attendance during part of the Baruch program (coincidental to her being in the US at time). As a result, the Baruch program was tailored nicely for to the Indian participants. This customized program at Baruch was used instead of an off-the-shelf program at NYIF thereby assuring better results for the participants.

Immeasurable training takes place when consultants meet with senior managers of one of the organizations to be improved. Some of this can be gleaned from trip reports. E.g., Cliff Kennedy had long meetings with SEBI on September 28 and 29, 1995 while he was in India working on strengthening the enforcement capabilities of the BSE, NSE and OTCEI. Lew Mendelsohn conducts a form of training when he spends long hours with the officials of the Association of Mutual Funds explaining the nuances of industry codes of professional standards. These one-on-one and working session types of interactions between the consultants and the involved Indians are built into the FIRE project by its director, and are emphasized as an element of the consultancy.

Conclusions and recommendations

While the FIRE project has provided much effective training to date, it is not clear to what extent training has been institutionalized. AMFI has conducted useful training programs, but the spur has been the FIRE project. Very valuable workshops have been sponsored by AMFI, with good participation from the membership and interested others. These programs, however, are special, high-profile events. SEBI has conducted similar programs. The stock exchanges, however, seem to be developing continuing, more routine, training activities in-house.

In the remaining time under the PW contract, it is recommended that the FIRE project increase its emphasis on institutionalizing the training activities of SEBI and the SROs. The chartered financial analysts professional society, for example, has discussed with PW its programs for training progressions that lead to successively higher levels of certification. Whatever the merits of the particular group and its specific programs, this model--of a continuing professional training/education--should be adopted more widely. It is important to develop skills on progressively increasing levels of sophistication throughout the capital market institutions. This is most likely to be achieved in stages.

General Conclusions and Recommendations

1. **The FIRE project is clearly in furtherance of the strategic objectives set forth in the Strategic Objective Tree.**

- The stated strategic objective is to reform the financial sector in order to increase the mobilization of capital. The PW component is addressed to *improving financial market efficiency.*

- Market efficiency implies that funds flow on the basis of informed evaluations of risk and potential return. Transaction costs are a function of market efficiency. In the Indian market, the clearing and settlement "costs" are major elements of transaction cost because of processing delays, fraud and counter party risk. The chances for a default or financial failure by some link in the process is especially acute in India because of the extensive number of sub-brokers spread throughout the country who are part of the system. In addition, the counterfeiting of share certificates is unusually common in India.

- Accordingly, PW has focused on:
  -modernizing systems to promote the efficiency of the capital markets,
  -reducing the current high levels of risk arising out of system inadequacies,
  -improving the protection of investors and enhancing liquidity in the equity and debt markets.
  -improving securities market transparency,

2. Program has had clear, positive impact.

The FIRE project has already made a significant and demonstrable impact on the development of India's financial markets. Once the Indian government made the commitment to financial market development that underpins the project, it became important for Indian participants in the financial system to have a source of guidance on how to effect that development. The FIRE project has provided that guidance.

Among the evidence of the FIRE project's effectiveness are the following:

- SEBI's role as an effective, credible regulatory agency has been established;
- Specific institutions are in place and operating to do what is expected of them and to produce the desired results in the market and for the economy: clearing/settlement, depository, better stock exchanges, better supervised market participants;
- The concept of self-regulation has begun to take root in India, and that is a major cultural adaptation;
- Both the government agencies and the private sector institutions look to the FIRE project for assistance and guidance, and the advice provided by the FIRE project director and consultants is given great weight in both sectors;
- Senior officers of SEBI and of private sector capital market institutions consistently affirm how valuable and important the training and guidance provided to them through the FIRE project has been in improving their effectiveness in their organizations;
- Daily newspaper accounts of some development in the capital markets that can be related to the FIRE project.

There is evidence that the equity markets are becoming a more significant element of India's financial system. In 1996, approximately 55% of the financial system's assets were intermediated through the capital market; 45% through the banks. By way of contrast, in 1990, the value of bank-intermediated assets was triple the value of assets intermediated in the equity-markets. This is not to suggest that the FIRE project is causally responsible for this development; it does suggest, however, that this is the right time for the FIRE project program to strengthen India's equity markets.

3. FIRE may need to re-examine its client relationships to draw clearer lines for when to initiate projects.

As the project was structured, SEBI appears to be the FIRE project's "client" or counterpart organization. As the project has evolved, however, there is some ambiguity in the SEBI - FIRE project relationship. For example, the SEBI chairman expressed to us that he does not always know what FIRE is doing. This was less a complaint than a statement in description of the relationship.

The project is working well and has been very effective. It is recommended that the relationship be continued in its present ambiguous form and that no action be taken to define the relationship more precisely. At the same time, it must be recognized that the FIRE project must balance between (i) only responding to SEBI's identification of problems/needs/approaches to solutions, and (ii) getting too far ahead of SEBI. The FIRE project director is to be commended for his discerning judgment in managing this balance successfully to date.

FIRE is operating under a level of effort contract. On the one hand, this provides an incentive to try to be all things to all critical institutions. On the other hand, if FIRE had to await decisions by SEBI or the GOI before launching projects or technical assistance undertakings, there no doubt would be a great deal of waiting and wasted time. This is a further argument in favor of avoiding more precise definition of the FIRE project relationship to SEBI and other capital market institutions. The oversight of the FIRE project by USAID through the approval and review of work plans, task orders and projects provide adequate safeguards and control.

It is recommended that USAID review with PW what the priorities should be for the rest of the project. For example, Is additional detailed technical assistance needed for the depository and clearing/settlement systems? If so, how much? Are these institutions now capable of providing for themselves the additional technical assistance they may need?

4. USAID should review the adequacy and applicability of its project performance indicators.

The project performance indicators set forth in the Strategic Objective Tree ("SOT") are objective measures of capital market expansion, such as increases in the number and value of shares traded, changes in the number of issuers and investors, increases in the number of company listings, and the like. PW has urged that alternative performance indicators, set forth in Appendix G, be used.

While we are not in a position to evaluate the specific performance indicators suggested by PW, the indicators set forth in the SOT should not be used as conclusive criteria for this project. In fact, they may be only anecdotal. Many, if not most, of the indicators are affected by market factors unrelated to the project's effectiveness.

The SOT indicators do not adequately measure the training aspects of the project, which are a very important element of the project. They do not adequately reflect the long-term developmental contribution of the project, such as institution building at SEBI or AMFI. As noted in this report, the project has had marked success in gaining acceptance in India for the concept of self-regulation in the securities industry. If this acceptance is sustained, and it appears to us that it will be, the project will have made a very significant contribution to India's financial sector development. Yet, the indicators do not undertake to measure this contribution.

Objective performance indicators cannot measure whether a project is well managed or whether the consultants have the cultural sensitivity necessary to be persuasive in their recommendations. These and other critical success factors must be left to the judgment of the USAID program officer in charge and to the project director of FIRE. If their judgments are poor, the project will not be salvaged by knowing that the number of shares held by households has increased over the past year

5. Suggested areas for FIRE to consider

- Technical assistance to explore and develop various forms of asset "securitization" in India as a means of enhancing liquidity positions of various financial institutions (e.g., leasing companies, factors, commercial banks, development finance companies, etc.). If a secondary market were developed for financial assets backed by various forms of otherwise relatively illiquid assets, it would increase the opportunities to create new financing arrangements. More and different assets could form the basis for securing finance, which would expand the array of business activities that could be financed externally. This could encourage new businesses to be created and existing businesses to expand and improve their efficiencies.

- Technical assistance for development of portfolio/fund management professionals. At present, mutual funds, pension funds and other large portfolios have few decisions to make. The financial assets available to them are limited in variety and number of issues within any class. In addition to reducing the investment returns for the beneficiaries of these funds, this situation means that the portfolios are not managed. Those responsible for the portfolios buy government securities and hold them to maturity and buy "blue chip" shares and hold them for the indefinite future.

  An active group of competitive, skilled portfolio managers could become a pressure group for policies conducive to capital market efficiency. The contrast between fund managers we met whose experience is limited to the Indian financial markets and those with experience in highly developed financial markets was striking to the evaluation team. The foreign-trained (usually in the U.S. or U.K.) understood the need for an active secondary debt market, for example, and were adding their voices to those advocating such a market. They were advocates for development of the post-trading systems in India. The Indian trained managers tend to be complaisant and unaware of how things could be different--or why they should be different.

  The FIRE project might consider portfolio management as a skill set in need of development and offer appropriate technical assistance and training to assist with the development.

- The FIRE project has much left to do and will probably need more time to do it. It is worth extending. The next directions should be deeper and broader.

  More deeply: into subsequent tiers: e.g., sub-broker issues, more work with SROs

  More broadly: both in geographical terms and in terms of complementary infrastructure development

  - Legal infrastructure
  - Expand varieties of financing available through capital market (as distinct from commercial banking sector)
  - Aside from the regional stock exchanges, what can be done to assure that the capital market is a national one? In this respect, the sub broker system may be an important element. It is not clear that there is adequate information and data about sub brokers and their role in the locales outside Bombay and Dehli.

Appendices

Business Standard, January 16, 1997

EXPERT OPTIONS

Secondary debt markets: a primary need

SIDHARATH KAPUR

Over the last one year, with the equity markets being lacklustre, investor interest has shifted to debt. The world over, retail investment is largely in debt instruments, and the fact that this is happening in India too is a sign of the maturing investor who has realised that equity risk, especially in greenfield projects with unknown promoters, is not his cup of tea. Debt instruments are safer, they offer a minimum yield with low risk of capital loss. However, the investor's love affair with debt can be sustained only if there is the development of a vibrant secondary market for debt.

The secondary market for debt lacks depth mainly because there are very few players. These are primarily banks and institutions. The bulk volumes are especially in gilt edged securities; corporate debt lacks volume. Most of the bulk deals are off market which are routed through the exchange only after they are concluded. In the past, there was a lack of critical mass as far as investors were concerned. This scenario has now changed.

A vibrant secondary market for debt is important since it imparts liquidity to the primary market investor. Investors hesitating to invest in long maturity instruments would not mind doing so when an exit option is available in the secondary market for such an instrument at any point during its tenure. This would open up new vistas for the debt market with investors who currently have a short term view opting for long term instruments. A secondary market would help investors overcome maturity mismatches and encourage investors to recycle investments in line with the movement of interest rates, change in rating and fresh investment avenues available. Investors would be able to take advantage of reducing their tax liability on account of income being charged as capital gain by selling in the secondary market (with special reference to deep discount bonds). An active secondary market would encourage corporates and high net worth individuals to deploy short term surpluses in secondary debt instruments.

When we look back over the past one year and see the large number of quality debt issues that have been subscribed by a larger number of retail investors, it cannot be disputed that there is now a mass of investors holding debt paper and their size is growing. In this scenario, proactive steps need to be taken to galvanise the secondary debt market. A larger numbers of players are needed for market making.

The IDBI Flexibond 2 issue is a step in the right direction since it addresses the liquidity problem by voluntarily coming forward to make a market for its instruments through intermediaries. While the IDBI prospectus does not mention the amount earmarked for market making, it is hoped that it is a reasonable amount (at least 5 per cent of the amount to be mobilised), in order to make it effective. Compulsory market making is needed in large debt issues of those, say, exceeding Rs 100 crores.

However, market making in OTC for equity has not succeeded, so how can it succeed in the retail debt segment? Firstly, repurchase of debt by the issuer is possible. Secondly, there are no volatile fluctuations in debt as are possible in equity. Therefore, if market making is done with limits and price fluctuation risk taken on by the issuer, it can succeed. It is the issuer who needs to earmark part of the proceeds (say 5 per cent) of the issue of offer quotes through market intermediaries. This would offer limited buyback to investors, and simultaneously activate the secondary market for that instrument with controlled risk on the issuer.

Apart from this, wide publicity needs to be given to secondary market debt options by newspapers and financial publications. Rating agencies need to publicise widely their rating watch and change in ratings. There is now a tendency to privately place debt with small investors, which is permitted to be listed on the wholesale debt market of NSE with a minimum trading lot of Rs. 5 lakh. Let us encourage the small investor investing in privately placed quality debt and permit listing of such debt with small trading lots.

Newer players need to be encouraged in corporate debt to enhance depth. Banks should be encouraged to increasingly invest in securitised corporate debt with an exclusive limit of, say, 5 per cent for investments. If provident funds and trusts can invest in PSU debt which is not rated or rated low, why should they not be permitted to invest a small percentage (say 5 per cent to 10 per cent) of investible resources in quality private sector debt with a minimum rating of "AA". This would open up a major investment window for corporate debt and the demand for debt in the primary and secondary markets would balloon.

Debt has emerged as a preferred investment option and is likely to continue to comprise a major portion of the funds raised through the capital market. It is high time the regulatory authorities, exchanges and government focused attention on the secondary debt market rather than being obsessed with equity alone.

Sidharath Kapur is senior vice president, Apple Finance. The views expressed here are those of the author.

APPENDIX B
List of persons interviewed

USAID
Ms. Linda Morse, Director, USAID
Mr. Desaix Myers, Deputy Director, USAID
Mr. Peter Thormann, Office of Economic Growth, USAID
Mr. Ashok Jha, Staff officer, USAID
Mr. Earl Kessler, Director, Regional Housing and Urban Development Office, USAID

US Embassy
Mr. Douglas Hartwick, Economic counselor, US Embassy, New Dehli
Mr. Curtis Stone, First Secretary (Economic), US Embassy, New Dehli
Ms. Neelu Kapoor, Economic specialist, US Embassy, New Dehli
Mr. Franklin Huddle, Jr., American consultate general

Dehli Stock Exchange
Mr. Paramjeet Singh, president
Mr. S.S. Sodhi, executive director
Mr. Vijay Bhushan, director and member

Bombay Stock Exchange
Mrs. Kalpana Maniar, deputy general manager, Bombay Stock Exchange
Mr. Vinod Patil, deputy general manager, surveillance, Bombay Stock Exchange
Mr. M.G. Damani, president, Mumbai (Bombay) Stock Exchange
Mr. R.C. Mathur, executive director, Mumbai Stock Exchange

Over the Counter Exchange of India
Mr. M. Pushpangadan, managing director, OTCEI

National Stock Exchange
Mr. Ravi Narain, deputy managing director, NSE
Ms. Chitra Ramkrishna, vice-president, NSE
Mr. Satish Naralkar, vice-president, NSE
Mr. Ashishkumar Chauhan, assistant vice president, NSE

Stockbrokers

Mr. Arjun Kapur, member DSE and member of committee on sub brokers
Mr. Milan Parekh, Action Financial Services (India) Ltd., member of BSE and NSE, member of NSDL, category II merchant banker, former sub-broker, research report publisher
Mr. Anand Rathi, managing partner, Anand Rathi & Co., member, Mumbai Stock Exchange
Mr. Sanat Dalal, member of Mumbai Stock Exchange
Mr. Padmakant Devidas Shah, member of Mumbai Stock Exchange

FIRE project consultants
Mr. William Gorman, consultant, PW FIRE
Mr. Lewis Mendelsohn, consultant, PW FIRE
Mr. Paul Litteau, consultant, PW FIRE
Mr. Thomas Keyes, consultant, PW FIRE
Mr. Walter Pugh, consultant, PW FIRE
Mr. Howard Malamud, consultant, PW FIRE
Ms. Rosemary McFadden, consultant, PW FIRE

FIRE project management

Mr. Dennis Grubb, Project director, FIRE
Mr. N. Sankaranarayanan, PW FIRE, office manager
Ms. Kim Shaak, PW FIRE training specialist

SEBI

Mr. D.R. Mehta, chairman, SEBI
Mr. L.K. Singhvi, executive director, SEBI
Mr. O.P. Gahrortra, senior executive director, SEBI

Reserve Bank of India

Mr. K. Kanagasabapathy, director, RBI internal debt management cell
Mr. Susobhan Sinha, manager, RBI internal debt management cell
Mr. T. Bandyopadhyay, chief officer, RBI department of financial companies
Mr. M.M. S. Rekhrao, chief general manager, RBI financial institutions cell
Mr. Janak Raj, director, RBI financial institutions cell

Ministry of Finance, GOI

Hon. U. Sarat Chandran, joint secretary, Ministry of Finance

Local training/education facilities

Institute of Chartered Financial Analysts of India

Mr. Subhash Sarnikar, Executive Director, Institute of Chartered Financial Analysts of India
Mr. Sangeetha Murthy, business school, Institute of Chartered Financial Analysts of India, Mumbai
Ms. Sanjeev Varma, analyst, Institute of Chartered Financial Analysts of India

Indira Gandhi Institute of Development Research

Mr. Ajay Shah, assistant professor, Indira Gandhi Institute of Development Research
Ms. Susan Thomas, research assistant, Indira Gandhi Institute of Development Research

Mutual funds and AMFI

Mr. K.N. Atma Ramani, managing director, Tata Asset Management Ltd., the Association of Mutual Funds in India
Mr. S.V. Mokashi, executive administrator, Association of Mutual Funds in India
Mr. A.P. Kurien, advisor, Apple Asset Management, Ltd., chairman, investor awareness committee, AMFI (developed a strategy paper on investor education)
Mr. Ajay Kakar, general manager, Obilvy & Mather, publicity advisers to the Association of Mutual Funds in India
Mr. Ajeet Prasad, general manager, Unit Trust of India

Major capital market institutions

Dr. S.A. Dave, advisor, Industrial Development Bank of India
Mr. Stephen Van Wilberding, DSP Merrill Lynch
Mr. Andy Doves, Jardine Fleming India Securities, Ltd.
Mr. Ajai Kaul, president and country manager, Alliance Capital Asset Management (India) Private Ltd.

Securities depository related organizations

Mr. C.B. Bhave, managing director, National Securities Depository Ltd.
Mr. V.R. Narasimhan, vice president, National Securities Depository Ltd.
Mr. T. Koshy, vice president, National Securities Depository Ltd.
Mr. R. Chandrasekaran, managing director, Stock Holding Corporation of India, Ltd.
Mr. L. Viswanathan, sr. vice president (finance), Stock Holding Corporation of India, Ltd.

Merchant banks

Mr. P. Chandrasekhar, AMBI representative and principal, Erudite Capital Creations, Ltd., merchant bankers

Mr. Asit Mehta, managing director, Asit Mehta investment intermediaries

Mr. Nimesh Kampani, chairman, JM Financial & Investment Consultancy Services, Ltd. and chairman of AMBI

Others

Cyril Shroff, Esq., Amarchand & Mangaldas & Hiralal Shroff & Co., solicitors and advocates

Mr. Subodh Shah, executive director, Credit Rating Information Services of India, Ltd.

APPENDIX C

List of PW FIRE consultants' activities

List of activities of the visiting US Consultants
Work Plan - First Year

Sr. No.	Name of the consultant	Period	Activity
1.	Mr. Richard Breen	February 6 - March 3, 1995	Support Module - U.S.
2.	Mr. Howard Schuman	March 27 - April 12, 1995	Training Needs Assessment
3.	Mr. Richard Breen	March 27 - April 21, 1995	Support Module - U.S.
4.	Mr. Julio Alcaine	April 4 - April 21, 1995	Training Needs Assessment
5.	Mr. John Ruckrich	May 12 - June 8, 1995	SHCIL - NCDS RFP
6.	Mr. William Rini	June 3 - June 10, 1995	Training Needs Assessment
7.	Mr. Howard Schuman	June 6 - June 21, 1995	Training Needs Assessment - analysis of questionnaire
8.	Mr. Richard Breen	June 3 - June 28, 1995	Support Module - U.S.
9.	Mr. Stephen Brown	June 1 - July 5, 1995	NSE - Debt Market Study
10.	Mr. Walter Pugh	July 13 - August 4, 1995	NSE - Computer Security and Disaster Recovery
11.	Mr. Richard Breen	August 14 - September 1, 1995	Support Module - U.S. - SEBI Conference and SHCIL - NCDS - RFI
12.	Mr. Auguste E. Rimpel, Jr	August 14 - August 22, 1995	Project Review
13.	Mr. Howard Schuman	August 20 - August 30, 1995	SEBI capital Markets Seminar and Executive Development Program
14.	Mr. Ranjit Advani	August 16 - September 7, 1995	NSE - Review of Back Office Systems
15.	Mr. Walter Pugh	August 23 - September 14, 1995	NSE - Computer Security and Disaster Recovery
16.	Mr. John Ruckrich	September 6 - October 8, 1995	SHCIL - NCDS Evaluation of RFI responses

17.	Mr. Cliff Kennedy	September 11 - October 6, 1995	SEBI - Review of Enforcement Plan and SRO status
18.	Mr. Frank Wilson	September 11 - September 26, 1995	NSE - Review of rules and regulations (SRO)
19.	Mr. Jeremiah O'Connell	September 16 - September 23, 1995	SHCIL - Global Securities Trading Seminar
20.	Mr. John Ruckrich	October 26 - November 11, 1995	SHCIL - NCDS Evaluation of RFI responses

List of activities of the visiting US Consultants
Work Plan - Second Year

Sr. No.	Name of the consultant	Period	Activity
1.	Mr. Ranjit Advani	November 14 - November 17, 1995	NSE - Review of Back Office Systems
2.	Ms. Jan Aalbregtse	November 16 - November 21, 1995	SEBI - Depository regulation
3.	Mr. Richard Breen	November 25 - December 15, 1995	SHCIL - NCDS Development of a Business Plan
4.	Mr. Terrance O'Malley	November 13 - December 20, 1995	SEBI - Review of enforcement Procedures
5.	Mr. Thomas R. Keyes	November 28 - December 20, 1995	SEBI - Broker Licensing and Certification
6.	Mr. Thomas R. Keyes	January 10 - January 25, 1996	SEBI - Broker licensing and certification
7.	Dr. William Barclay	January 21 - February 2, 1996	NSE - Futures and Options trading
8.	Frank Wolf	December 1- February 2, 1996	Derivatives Feasibility study
9.	Mr. John Ruckrich	January 5 - February 4, 1996	NSE - Securities Depository RFP
10.	Mr. Walter Pugh	January 31 - February 12 and February 20 - March 1, 1996	SHCIL - Computer Security and Disaster recovery
11.	Mr. William Dentzer	February 11 - February 16, 1996	SEBI Depository regulations
12.	Mr. Dick Breen	February 11- February	
13.	Mr. Clifford Kennedy	February 11 - March 5, 1996	Review of SEBI enforcement Program
14.	Mr. John Ruckrich	March 1 - March 15, 1996	NSE Study Tour - Site visit of vendors and Vendors' Question and Answer session held at NSE Head Quarters
15	Mr. John Ruckrich	February 26 - March 27, 1996	NSDL Business Planning and NSE Study tour

16	NSE	March 4 - March 15, 1996	NSE - Study Tour - Site visit of vendors
17	Mr. Ranjit Advani	March 20 - 26, 1996	NSE - Back Office System Review
18	Mr. Frank Wilson	April 3 - 24, 1996	NSE - Review of rules and regulations of NSE and its status as a self regulatory organization
19	Mr. Walter D. Pugh	April 10 - 24, 1996	NSE - Computer Security and Disaster recovery
20	Mr. Thomas R. Keyes	March 28 - May 2, 1996	Broker Licensing and Certification Program
21	Mr. Cliff Kennedy	April 1 - May 4, 1996	SEBI enforcement program
22	Mr. John Ruckrich	April 30 - May 17, 1996	Depository Regulation Review and NSDL bye laws co-ordination
23	Ms. Jan Aalbregtse Slinn	May 1- 17, 1996	NSDL - Depository regulation Review and NSDL bye laws co-ordination
24	Mr. Thomas R. Keyes and Mr. Paul	May 13 - May 15, 1996	Broker Licensing and Certification assistance to SEBI
25.	Mr. Bill Gorman	May 12 - 25, 1996	SEBI Australasia Depository Study tour
26.	Mr. Frank Wilson	June 8 - June 27, 1996	NSE SRO program and SEBI Stock Watch and SRO concept
27.	Ms. Susan J. Hertel	May 31 - July 6, 1996	Organizational Structure Plan for NSDL
28.	Mr. Cliff Kennedy	July 15 - August 20, 1996	Review of SEBI enforcement program, Workshop on Derivatives for NSE
29.	Mr. Lewis Mendelson	July 19 - August 18, 1996	Assistance to Mutual Funds
30.	Mr. Walter Pugh	August 16 - September 5, 1996	Computer security and disaster recovery planning for NSE & SHCIL
31.	Ms. Jan Aalbregtse Slinn	August 29 - September 13, 1996	NSDL bylaws
32.	Ms. Susan J. Hertel	August 2 - September 15, 1996	NSDL work flows and job descriptions

33.	Mr. Thomas R. Keyes	August 15 - September 26, 1996	Broker licensing and certification
34.	Mr. Paul Litteau	September 23 - October 5, 1996	Derivatives regulation and orientation
35.	Mr. John Ruckrich	September 6 - October 12, 1996	Depository rules and regulations
36.	Ms. Jan A. Slinn	October 12 - 25, 1996	NSDL Depository participant agreements

List of activities of the visiting US Consultants
Work Plan - Third Year

Sr. No.	Name of the consultant	Period	Activity
1.	Mr. Lew Mendelson	October 10. - November 10, 1996	Assistance to AMFI
2.	Ms. Susan Hertel	October 17 - November 16, 1996	NSDL organizational work flow activities
3.	Mr. Cliff Kennedy	November 1 - 22, 1996	Enforcement and Surveillance program for SEBI
4.	Mr. Joseph Schenk	November 3 - 22, 1996	Clearing and settlement corporations for BSE and DSE
5.	Mr. Bill Gorman	November 17 - December 2, 1996	Inter connectivity of Stock Exchanges
6.	Mr. John Ruckrich	November 30 - December 20, 1996	NSDL operational procedures
7.	Mr. Frank Wolf	June 19 - December 4, 1996	Depository cost studies for BSE and DSE
8.	Ms. Jan Aalbregtse Slinn	December 2 - 18, 1996	NSDL byelaws
9.	Mr. Bill Gorman	January 3 - 21, 1997	Inter connectivity of Stock Exchanges
10.	Paul Litteau	Presently working	Derivatives Exchange
11.	Walter Pugh	Presently working	Business continuity plan
12.	Lew Mendelson	Presently working	Mutual Fund program
13.	Harry Melamad	Presently working	Broker accountability and system development
14.	David Silver	Presently working	Mutual Fund awareness program
15	Sue Hertel	Presently working	Depository training program
16	Rosemary McFadden	Presently working	Derivatives program
17	Tom Keyes	Presently working	Broker certification program
18	Joseph Schenk	Presently working	claering and settlement corporations

APPENDIX D

Performance analysis of PW FIRE project prepared by PW

Performance Analysis of FIRE Project

Activity Component	Workplan I (11/15/94 - 10/31/95)			Workplan II (11/01/95 - 10/31/96)			Cumulative 11/94 - 10/96 (for 23.5 months)		
	Projected	Delivered	Performance	Projected	Delivered	Performance	Projected	Delivered	Performance
US Training (person weeks)	32	39.4	123.13%	88.4	89.4	101.13%	120.4	128.8	106.98%
In-country training (person weeks)	257	119	46.30%	767	723	94.26%	1024	842	82.23%
U.S. Tech. Assistance (person months)	41	12.9	31.46%	33.8	28	82.84%	74.8	40.9	54.68%

Activity Component	Cumulative 11/94 - 10/96 (for 23.5 months)			Workplan III (11/01/96 - 10/31/97)			Cumulative 11/94 - 10/97 (for 35.5 months)		
	Projected	Delivered	Performance	Projected	Delivered	Performance	Projected	Delivered	Performance
US Training (person weeks)	120.4	128.8	106.98%	252	252	100.00%	372.4	380.8	102.26%
In-country training (person weeks)	1024	842	82.23%	759	759	100.00%	1783	1601	89.79%
U.S. Tech. Assistance (person months)	74.8	40.9	54.68%	93.33	93.33	100.00%	168.13	134.23	79.84%

Assuming only 50% of the projections in the Third plan is achieved, the scenario will be as below at the end of the III Plan

Activity Component	Cumulative 11/94 - 10/96 (for 23.5 months)			Workplan III (11/01/96 - 10/31/97)			Cumulative 11/94 - 10/97 (for 35.5 months)		
	Projected	Delivered	Performance	Projected	Delivered	Performance	Projected	Delivered	Performance
US Training (person weeks)	120.4	128.8	106.98%	252	126	50.00%	372.4	254.8	68.42%
In-country training (person weeks)	1024	842	82.23%	759	380	50.07%	1783	1222	68.54%
U.S. Tech. Assistance (person months)	74.8	40.9	54.68%	93.33	47	50.36%	168.13	87.9	52.28%

Activity Component	Cumulative 11/94 - 10/96 (for 23.5 months)			End of Workplan III (11/01/96 - 10/31/97) @ 100% performance in III Plan			End of Workplan III (11/01/96 - 10/31/97) @ 50% performance in III Plan		
	Projected	Delivered	Performance	Project target	Delivered	Performance	Project target	Delivered	Performance
US Training (person weeks)	120.4	128.8	106.98%	176	380.8	216.36%	176	254.8	144.77%
In-country training (person weeks)	1024	842	82.23%	2070	1601	77.34%	2070	1222	59.03%
U.S. Tech. Assistance (person months)	74.8	40.9	54.68%	154	134.23	87.16%	154	87.9	57.08%

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Estimated Input of Expatriate Consultants' Level of Efforts (in weeks)
(November 1995 - April 1997)

Activity	1995	1996		1997	Total LOE
	Till Oct	Till May	Till Oct	Till Apr	
I. Depositories/ Clearing Corporations					
National Depository system Develop program, review rules, etc.	5	22	13	1	41
NSDL Operational staff training	1		4	5	10
Establish awareness in Fin. community				3	3
NSDL Business expenditure forecast plan	6			2	8
Information systems - data security & Back office review	13	8	9	8	38
Consolidated Tape - feasibility study of NSMS				18	18
Clearing and settlement Corporation for NSE & RExgs			10	11	21
Activities with OTCEI & RExgs			6	16	22
Develop awareness among market intermediaries				18	18

Activity	1995 Till Oct	1996 Till May	1996 Till Oct	1997 Till Apr	Total LOE
II. A. SRO Activities					
Orgn. Development Strategy for SEBI			4	1	5
SRO - Initiate discussion and deliver seminars	3	3	2	13	21
II. B. Broker Certification					
Evaluate methodology for the introduction of licensing program		3		10	13
Develop an Examination System and Administer Test		3		23	26
Design and implement Core curriculum for Broker certification		4	2	20	26
II. C. Investor Information Centers					
Design implement Investor Information Center concept (Design)			3	1	4
Design implement Investor Information Center concept (IT)			2	3	5
III. Debt market Development					
Debt Market - workshops	10		9	17	36

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Activity	1995	1996		1997	Total LOE
	Till Oct	Till May	Till Oct	Till Apr	
IV. Enforcement & Market Surveillance					
Technical Assistance to develop regulations	5	8	1	18	32
Design Implement Surveillance, etc., Plan	5	5	2	7	19
V. Futures/ Options Exchange					
Derivatives Exchange		10	6	15	31
VI. Investor Base/ Mutual Funds					
Develop regulations for MFs/ MFSRO				18	18
VII. Others					
Develop relationship with new institutions	19		8	3	30
Research topics for participating institutions				5	5
SDDS Activities			2	2	4
Total Input	**67**	**66**	**83**	**238**	**454**

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APPENDIX E

Summary of completed FIRE project training activities

November 1994 - January 1997

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Completed Training
November 1994-January 1997

No.	No. of Persons	Home Organization	Program Length	Person Weeks	Timing	Workshop/Seminar/Instructor
1.	*26	NSE	2 days	10pw	May 19-20, 1995	*Futures and Options Market* Anil Narang, Sanjay Soni
2.	*62	SEBI	3 days	37pw	August 26-28, 1995	*Organizational Development* Howard Schuman
3.	*8	SHCIL	½ day	1pw	September 25, 1995	*Software Vendor Selection Process* John Ruckrich
4.	*22	SEBI Division Chiefs	1 day	5pw	September 28, 1995	*Enforcement and SRO's* Cliff Kennedy
5.	*22	Stock Exchanges and SEBI	1 day	5pw	September 29, 1995	*Enforcement and SRO's* Cliff Kennedy
6.	*60	UTI Instit. of Cap Markets	½ day	6pw	October 1995	*Depository Development* W. Dennis Grubb
7.	*93	SHCIL	3 days	55pw	October 1995	*Global Security Services* Jerry O'Connell
8.	51	IMC Stock Market	½ day	5pw	December 1995	*Depository* W. Dennis Grubb
9.	5	UTI Inst. of Capital Markets	1 day	1pw	December 13, 1995	*Licensing and Certification* Tom Keyes
10.	8	SEBI Licensing Com	1 day	2pw	December 1995	*Licensing and Certification* Tom Keyes
11.	184	AMF Fin Services Convention	½ day	18pw	January 1996	*Depository Developmentl* W. Dennis Grubb
12.	76	Rotory	½ day	7pw	January 1996	*The Share Market Bank* W. Dennis Grubb
13.	8	SEBI	½ day	1pw	January 1996	*Enforcement Procedures* Terrance O'Malley

No.	No. of Persons	Home Organization	Program Length	Person Weeks	Timing	Course/Instructor
14.	11	USAID, ADB, Delhi Stock Exchange	½ day	1pw	January 31, 1996	*Financial Futures and Options* Dr. William Barclay
15.	70	NSE, SEBI, Banks, Brokers	1 day	14pw	February 2, 1996	*Financial Futures and Options* Dr. William Barclay
16.	25	Custodians	½ day	2pw	February 15,.1996	*Depository* William Dentzer
17.	12	ICICI	½ day	1pw	February 15, 1996	*Depository* William Dentzer
18.	18	Brokers and Custodians (Jardine, DSP, BSE)	½ day	2pw	February 16, 1996	*Depository* William Dentzer
19.	50	Conference Board	½ day	5pw	February 16, 1996	*Depository* William Dentzer
20.	16	OTCEI	½ day	2pw	February 1996	*Data Security* Wally Pugh
21.	10	SHCIL	½ day	1pw	February 1996	*Data Security* Wally Pugh
22.	31	SEBI, Regional Exchanges	1day	6pw	March 1996	*Securities Enforcemtn and Self Regulation* Cliff Kennedy
23.	10	SEBI Regional Offices Madras	1day	2pw	April 1996	*Securities Enforcement and Self Regulation* Cliff Kennedy
24.	5	SEBI	1 day	1pw	April 1996	*Self Regulatory Organizations Rules and Regulations* Frank Wilson
25.	148	NSE Members	1day/each	30pw	April 1996	*Self Regulatory Organizations Rules and Regulations* Frank Wilson
26.	5	OTCEI	1day	1pw	April 1996	*Self Regulatory Organizations Rules and Regulations* Frank Wilson
27.	41	NSE, OTC	1days	8pw	April 1996	*Information Security Awareness Training* Wally Pugh & Citibank
28.	26	NSE, OTC	1 days	5pw	April 1996	*Data Security Training* Wally Pugh & Citibank

No.	No. of Persons	Home Organization	Program Length	Person Weeks	Timing	Course/Instructor
29.	75	Madras Sub-Brokers	1day	15pw	April 20, 1996	*"Sub-Broker" Workshop* Tom Keyes
30.	70	Individual Madras Investors	1day	14pw	April 19,1996	*Investor Education Workshop* Tom Keyes
31.	50	Madras Exchange/ Brokers	1 day	10pw	April 1996	*Investor Education and Structural Changes* Tom Keyes
32.	5	OTCEI	1day	1pw	April 1996	*Depository Workshop* Wally Pugh
33.	4	SEBI	1 day	1pw	April 1996	*Self Regulation In the Securities Industry* Cliff Kennedy
34.	14	SEBI Regional Office Delhi	1day	3pw	May 2, 1996	*Securities Enforcemtn and Self Regulation* Cliff Kennedy
35.	10	NSE Participants	½ day	1pw	May 1996	*Rules and Regulations for Depository* John Ruckerich and Jan Slinn
36.	85	Invest India Stock Exchanges Summit Participants	½ day	8pw	May 1996	*Global Experience of Stock Exchanges* W. Dennis Grubb
37.	90	Invest India Stock Exchanges Summit Participants	½ day	9pw	May 21, 1996	*Expectations of Depositories* W. Dennis Grubb
38.	50	Calcutta	1 day	10pw	May 1996	*Sub Broker Workshop* W. Dennis Grubb/Paritosh Sharma
39.	70	Calcutta	1 day	14pw	May 1996	*Individual* Investor W. Dennis Grubb/Paritosh Sharma
40.	12	NSDL	1/2 day	1pw	July 20, 1996	*Organizational Structure* Sue Hertel
41.	*65	USIS Guests	1 day	13pw	July 23, 1996	*Financial Sector Reforms: It is Time to Move On* Dr. Richard Erb

No.	No. of Persons	Home Organization	Program Length	Person Weeks	Timing	Course/Instructor
42.	*25	Indo-American Chamber of Commerce	1/2 day	5pw	July 1996	*Reforms Required In The Indian Capital Markets to Meet International Standards* Dennis Grubb
43.	126	NSE Brokers Bombay	1 day	25pw	July 20, 1996	*Derivatives Orientation Programme* Cliff Kennedy/W. Dennis Grubb
44.	97	NSE Brokers Bombay	1 day	19pw	July 21, 1996	*Derivatives Orientation Programme* Cliff Kennedy/ W. Dennis Grubb
45.	109	NSE Brokers New Delhi	1 day	22pw	July 27, 1996	*Derivatives Orientation Programme* Cliff Kennedy
46.	106	NSE Brokers New Delhi	1 day	21pw	July 28, 1996	*Derivatives Orientation Programme* Cliff Kennedy
47.	20	PW Comptroller/ Auditor Seminar New Delhi	2 days	8pw	July 30-31, 1996	*Development in the Capital Markets, Surveillance and Enforcement Activities* Cliff Kennedy & W. Dennis Grubb
48.	85	Custodians & Banks Bombay	1/2 day	9pw	July 30, 1996	*NSDL Depository Workshop* W. Dennis Grubb
49.	70	Registrars & Issuers Bombay	1/2 day	7pw	July 30, 1996	*NSDL Depository Workshop* W. Dennis Grubb
50.	65	Brokers & Dps Bombay	1/2 day	6pw	July 30, 1996	*NSDL Depository Workshop* W. Dennis Grubb
51.	23	AMFI	1/2 day	2.3 pw	August 1, 1996	*AMFI Education Seminar* Lew Mendelson
52.	102	NSE Brokers Madras	1 day	20.4pw	August 3, 1996	*Derivatives Orientation Programme* Cliff Kennedy
53.	98	NSE Brokers Calcutta	1 day	19.6pw	August 4, 1996	*Derivatives Orientation Programme* Cliff Kennedy
54.	25	SEBI	1 day	5pw	August 1996	*Enforcement and Regulatory Workshop* Cliff Kennedy
55.	67	Registrars & Issuers, Custodians & Banks Ahmedabad	1 day	13pw	August 6, 1996	*NSDL Depository Workshop* W. Dennis Grubb

No.	No. of Persons	Home Organization	Program Length	Person Weeks	Timing	Course/Instructor
56.	106	Registrars & Issuers, Custodians & Banks New Delhi	1 day	21pw	August 9, 1996	*NSDL Depository Workshop* Sue Hertel
57.	60	NSE Brokers Ahmedabad	1day	12pw	August 10,1996	*Derivatives Orientation Programme* Cliff Kennedy
58.	16	AMFI	1/2 day	1.6pw	August 13, 1996	*AMFI Eduction Seminar* Lew Mendelson
59.	58	Registrars & Issuers Custodians & Banks Hyderabad	1 day	11.6pw	August 14, 1996	*NSDL Depository Workshop* W. Dennis Grubb
60.	29	SEBI New Hires	1 day	5.8pw	August 14, 1996	*Orientation to Surveillance, Enforcement* Cliff Kennedy
61.	117	NSE Brokers Bombay	1 day	23pw	August 17, 1996	*Derivatives Orientation Programme* Cliff Kennedy
62.	123	NSE Brokers Bombay	1 day	24pw	August 18, 1996	*Derivatives Orientation Programme* Cliff Kennedy
63.	88	Registrars, Issuers, Custodians & Banks Calcutta	1 day	17.6pw	August 21, 1996	*NSDL Depository Workshop* W. Dennis Grubb
64.	52	Registrars, Issuers, Custodians & Banks Madras	1 day	10.4pw	August 26, 1996	*NSDL Depository Workshop* W. Dennis Grubb
65.	43	Registrars& Issuers Bangalore	1 day	9.6pw	August 29, 1996	*NSDL Depository Workshop* W. Dennis Grubb
66.	6	SHCIL	1 day	1.2pw	August 30, 1996	*Information Systems/Back Office Operations and Business Continuity Planning* Wally Pugh
67.	2	NSDL	1day	.4pw	August 31, 1996	*Communications and Work Flows* Sue Hertel

No.	No. of Persons	Home Organization	Program Length	Person Weeks	Timing	Course/Instructor
68.	7	NSE	1 day	1.4pw	September 2, 1996	*Information Systems/Back Office Operations and Business Continuity Planning* Wally Pugh
69.	*200	Conference Participants	1/3 day	13.3 pw	September 6, 1996	*Lala Institute for Management Studies* W. Dennis Grubb
70.	*100	Institute of Company Secretaries of India	1 day	20pw	September 6, 1996	*Law Relating to Depositories* Jan Slinn
71.	16	SEBI Exchanges	1/2 day	1.6pw	September 17, 1996	*Sub Broker Accessibility* Tom Keyes
72.	60	Sub -Brokers Delhi	1/2 day 4p.m.- 7p.m.	6pw	September 19, 1996	*Securities Intermediaries* Tom Keyes/Paritosh Sharma
73.	5	DSE	1 day 10-7	1pw	September 19, 1996	*Securities Intermediaries* Tom Keyes/Paritosh Sharma
74.	150	Sub-Brokers Bombay	1/2day	15pw	September 21, 1996	*"Sub-Broker" Workshop* Tom Keyes/Paritosh Sharma
75.	479	BSE Sub Brokers	1/2 day	47.9 pw	September 23, 1996	Indian Association of Securities Intermediaries Tom. Keyes/Paritosh Sharma
76.	31	Market Participants	2 days	12.4 pw	September 25-26, 1996	*Derivatives Workshop* Paul Litteau & Monika Jaislani
77.	20	AMBI	1/2 day	2pw	September 25, 1996	Tom Keyes
78.	27	Market Participants	2 days	10.8pw	September 27-28, 1996	*Derivatives Workshop* Paul Litteau & Monika Jaislani
79.	15	SEBI	1 day	3pw	October 1, 1996	*Derivatives Workshop* Paul Litteau & Monika Jaislani
80.	125	Small Investors Maduri	1/2 day	12.5	October 5, 1996	*Recent Developments in Indian Capital Markets* Sankaranarayanan

No.	No. of Persons	Home Organization	Program Length	Person Weeks	Timing	Workshop/Seminar/Instructor
81.	25	American College Management Students/ Faculty Madurai	1/2 day	2.5pw	October 5, 1996	*Emerging Capital Markets Scenario* Sankarananarayanan
82.	200	Brokers Mumbai	1 day	40pw	October 5, 1996	*Stress Management for Stock Brokers* W. Dennis Grubb
83.	30	Indo American Society	1 day	6pw	October 19, 1996	*Winds of Change* W. Dennis Grubb
84.	40	Unit Trust of India	1/2 day	4pw	October 28, 1996	Futures and Options W. Dennis Grubb
85.	35	CERC	1/2 day	3.4pw	November 1, 1996	*Economic Liberalization* W. Dennis Grubb
86.	250	ASAF / ICFAI	1/2 day	25pw	December 3, 1996	*Infrastructure Development in Indian Capital Market* W. Dennis Grubb
87.	200	Institute of International Consultants Hyderbad	1/2 day	20pw	December 7, 1996	*International Consulting on Capital Markets W. Dennis Grubb*
88.	5	Coimbatore Exchange Executives	1 day	1pw	January 2, 1997	*Future of the Sub Broker Tom Keyes & Paritosh Sharma*
89.	50	Coimbatore Sub Brokers	1/2 day	5pw	January 3, 1997	*Future of the Sub Broker Tom Keyes & Paritosh Sharma*
90.	60	Madras Sub Brokers	1/2 day	6pw	January 4, 1997	*Future of the Sub Broker Tom Keyes & Paritosh Sharma*
91.	5	Madras Exchange Executives	1 day	1 pw	January 5, 1997	*Future of the Sub Broker Tom Keyes & Paritosh Sharma*
92.	5	Hyderabad Exchange Executives	1/2ay	.5	January 5, 1997	*Future of the Sub Broker Tom Keyes & Paritosh Sharma*
93.	190	Hyderabad Sub Brokers	1/2 day	19pw	January 6, 1997	*Future of the Sub Broker Tom Keyes & Paritosh Sharma*
94.	5	Bangalore Exchange Executives	1 day	1pw	January 7, 1997	*Future of the Sub Broker Tom Keyes & Paritosh Sharma*
95.	210	Bangalore Sub Brokers	1/2 day	21pw	January 8, 1997	*Future of the Sub Broker Tom Keyes & Paritosh Sharma*

No.	No. of Persons	Home Organization	Program Length	Person Weeks	Timing	Workshop/Seminar/Instructor
96.	5	Calcutta Exchange Executives	1 day	1pw	January 9, 1997	*Future of the Sub Broker* *Tom Keyes & Paritosh Sharma*
97.	350	Calcutta Sub Brokers	1/2 day	35pw	January 10, 1997	*Future of the Sub Broker* *Tom Keyes & Paritosh Sharma*
98.	300	Mumbai	1/2 day	30pw	January 15, 1997	*Individual Investor Awareness* *Sue Hertel & Kim Shaak*
99.	10	Ministry of Finance New Delhi	1/2 day	2pw	January 16, 1997	*The Role of Mutual Funds in the Development of India's Capital Markets* *David Silver & Lew Mendelson*
100	10	Round Table Discussion Capital Market Pariticipants New Delhi	1/2 day	2pw	January 16, 1997	*The Role of Mutual Funds in the Development of India's Capital Markets* *David Silver & Lew Mendelson*
101	5	Ahmedabad Exchange Executives	1/2 day	.5pw	January 16, 1997	*Future of the Sub Broker* *Tom Keyes & Paritosh Sharma*
102	200	Ahmedabad Sub Brokers	1/2 day	20pw	January 16, 1997	*Future of the Sub Broker* *Tom Keyes & Paritosh Sharma*
103	40	Mutual Funds Agents IDBI; IFCI New Delhi	1 day	8pw	January 17, 1997	*The Role of Mutual Funds in the Development of India's Capital Markets* *David Silver & Lew Mendelson*
104	5	Baroda Excahnge Executives	1/2 day	.5	January 18, 1997	*Future of the Sub Broker* *Tom Keyes & Paritosh Sharma*
105	130	Baroda Sub Brokers	1/2 day	13pw	January 18, 1997	*Future of the Sub Broker* *Tom Keyes & Paritosh Sharma*
106	400	Mumbai	1/2 day	40pw	January 18, 1997	*Individual Investor Awarness* *W. Dennis Grubb*
107	5	Jaipur Exchange Executives	1/2 day	.5pw	January 20, 1997	*Future of the Sub Broker* *Tom Keyes & Paritosh Sharma*
108	100	Jaipur Sub Brokers	1 day	20 pw	January 20, 1997	*Future of the Sub Broker* *Tom Keyes & Paritosh Sharma*
109	80	UTI Third Annual Mutual Funds Conference	1/2 day	16 pw	January 20, 1997	*The Role of Mutual Funds in the Development of India's Capital Markets* *David Silver & Lew Mendelson*

No.	No. of Persons	Home Organization	Program Length	Person Weeks	Timing	Workshop/Seminar/Instructor
110	20	AMFI	1/2 day	4pw	January 20, 1997	*The Role of Mutual Funds in the Development of India's Capital Markets* *David Silver & Lew Mendelson*
111	8	UTI Chairman & Executive Trustee& Directors	1/2 day	.8pw	January 21, 1997	*The Role of Mutual Funds in the Development of India's Capital Markets* *David Silver & Lew Mendelson*
112	80	UTI Third Annual Mutual Funds Conference	1/2 day	8pw	January 21, 1997	The Role of Mutual Funds in the Development of India's Capital Markets *David Silver & Lew Mendelson*
				1132.1 pw		

APPENDIX F

Copies of illustrative trainee reports

SECURITIES AND EXCHANGE BOARD OF INDIA

16/12/96

Enclosed please find our trip report on the training programme titled " Capital Markets" conducted at New York from October 28- November 15, 1996.

Sujit Prasad

N. BHARDWAJ   P.K. KURIACHEN   S. PRASAD   PARAG JAIN

R.V. NABAR

DC, IEMI

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A TRIP REPORT ON THE TRAINING PROGRAMME TITLED " CAPITAL MARKETS" CONDUCTED AT NEW YORK FROM OCTOBER 28-NOVEMBER 15, 1996.

A training program on "Capital Markets" in the U.S.A was organised by Baruch College, Division of Continuation Studies, City University of New York for the Indian Securities and Exchange Group at New York, U.S.A.

The training program was for a period of 3 weeks from October 28, 1996 to November 15, 1996. The program was organised under the aegis of the USAID/Fire Project. The program included lecture from a wide range cross-section of personalities involved in the capital markets and visits to several intermediaries/regulatory bodies (Self Regulatory and others) associated with the capital markets. The names of persons and organisations with which they are associated are given in the annexure. The main objective of the internship was to get an insight into the various aspects / facets of the capital market, with particular reference to the conditions prevailing in the U.S. Capital Markets.

The following paragraphs contain a gist of the various lectures given and visits made during the internship / training program.

I. Lecture by the Mr Peter W Greenough, Managing Director Greenough & Co, Inc.

Mr. Greenough, gave an introduction and overview of the capital markets in the U.S. The emphasis of the lecture was to give an introduction to the various players, intermediaries and regulators associated with the capital markets. He also discussed the various methods by which money flows in and out of the system and the methods adopted by the players to mitigate the risk involved in the transaction. The speaker also introduced the regulators in the capital market and their role in maintaining a fair and orderly market.

II. Financial Markets in the U.S.A. - Mr. Kishore Tandon

The speaker, Mr. Kishore Tandon gave an overview of the various instruments that are traded/ listed or floated by the companies to the investing public. The speaker also gave an introduction to the role of the specialists on the floor of the New York Stock Exchange and the procedure to the followed for private placements.

III. **Back Office Operations - Mr. Michael Curley.**

Mr. Michael Curley of Bear Stearns talked about the entire back office operations involved in a broking firm. He dealt with the different departments that are there in a brokerage firm and the functions performed by the various departments. The manner in which a sale or a buy order can be put across was also explained and the various operations on the floor of the NYSE or the NASDAQ was also explained. The impact of the various regulations imposed by the SEC and the Federal Reserve were also dealt with the speaker. It was a very informative session and an insight into the functioning of the various departments and divisions involved in the settlement of a trade.

IV. **Auditors Involvement with Publicly held Companies' Filings with the SEC. - Mr Edward Martin.**

The speaker, an auditor by profession, gave an introduction to the various documents that have to be filed by listed companies with the SEC. The accounts have to confirm to the Generally Accepted Accounting Practices (GAAP). All listed companies have to file the offer documents and also other documents on the performance of the company on a regular basis to the SEC. The role of the auditor in these filings as well as the procedure adopted by the SEC in verifying these documents was also explained.

V. **Clearing Issues in Derivatives Markets _ Mr. Terrence Martell**

The speaker, a person well versed with the derivatives markets gave an insight into the functioning of the commodities market and the method adopted in clearing and settling trades in an options market. The speaker gave an introduction as to what is meant by a futures contract and also explained the difference between a futures and a forward contract. The methods adopted in settling a futures contract was also explained. The functioning of the clearing house and the manner in which operates to settle / guarantee trades was also discussed at to get a good knowledge into the functioning of the futures and Cocoa Exchange which included a visit to the floor and a talk on the regulatory aspects in the exchange.

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VI. **Private Placements Markets in the U.S. - Mr. Juan Pajol.**

The talk was on the method of raising money in the private equity markets by Companies. Such issues are not required to be registered with the SEC. The issuers, the intermediaries and the process of raising money in the private equity market was discussed at length.

VII. **U S Equity Markets and the New York Stock Exchange _ Mr David Krell, Vice President, New York Stock Exchange**

The speech concentrated on the working of the New York Stock Exchange, the number of companies listed, the procedure to be adopted by the companies to list their shares on the NYSE, the various compliance procedures to be followed by the companies and the surveillance procedures followed by the NYSE. The role of specialists was also covered at length. A visit to the floor of the NYSE was also arranged. On the exchange, the regulatory and the surveillance departments gave a talk on the manner in which the surveillance functions are carried out by the NYSE.

VIII. **Visit to Bloomberg Business News**

Bloomberg Business News is a news agency which transmits news about the companies located all over the world on line to the subscribers. The data included the data included the date of incorporation, a brief history of the company, the financial data and the stock price movements. The database also included data on countries and the details of the bonds/debt issues. The manner of collecting data, the method of updating the data and the ways in which the data can be accessed by the subscribers was shown at length by the staff of Bloomberg.

IX. **Lecture by Mr. Philip Zweig - Business Week.**

Mr. Philip Zweig was formerly with the Wall Street Journal and has authored two books, one of the former chief of Citi Bank. He spoke on the manner in which Journalists collect news and report news items. He also shares a few personal experiences that he had while collecting news.

X. **Visits to the Federal Reserve**

The visits to the Federal Reserve Bank of New York was a general visits. The visit covered the way in which the Fed is organised and a visit to the gold reserve of the Fed.

XI. Visit to VZB Partners

VZB is a Hedge Fund which invests its surplus funds in a manner to mitigate the risk. The functioning of the hedge fund and the way in which the returns are distributed to the investor was discussed at length. The return for the hedge fund from the investment was also indicated. The problems facing the investment was also indicated. The problems facing the registration of hedge funds in India was also debated at length.

XII. Visit to Securities Industry Automation Corporation.

SIAC is an intermediary which receives the physical certificates in case of ineligibles (i.e. those certificates which still exist in the physical form) from the brokers, destroy the old certificates and issue fresh certificates to the new holder, it was also learnt that SIAC is the sister company of the Depository Trust Company and does all the software and other software related work for the depositors and the clearing companies.

XIII. Visit to Nomura Securities

Nomura Securities is the second largest investment bankers in the world. At Nomura, corporate Finance was discussed from the regulatory and the broker perspective. Ms. Linda Quinn, formerly with the Corporate Finance Division of the U.S. Securities And Exchange Commission. She gave the audience an idea of the items looked at the SEC and the normal procedure adopted by the SEC while raising observations/ checking the disclosures in the offer document. Ms. Danelle Carbone of Shearman Sterling explained the steps taken by the investment bankers in filing offer documents with the SEC, the various queries raised by the SEC and the manner in which replies are forwarded and the final clearance obtained. Mr. Charles Whitehead and Scott Rockoff of Nomura Securities discussed the aspect of Corporate Finance from the brokerage perspective i.e. after the issue is open for subscription. The various safeguards to be adopted by the brokers and the method of marketing the issue as well as the pricing of the issue was discussed at length in this section.

XIV. Visit to the Securities Training Corporation.

The Securities Training Corporation imparts training to the various intermediaries associated with the capital markets, who in turn have to undergo different types of exams, depending on the type of job to be performed. The speaker also informed of the two types of forms that have to be filed by every broker with the Central Registration Depository (U - 4 and U - 5) and the purpose of these forms.

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XV. Visit to the Emerging Markets Week / Institutional Invested Magazine

Emerging Markets is a magazine which covers the developing nations / Emerging markets. The manner of gathering news as well the topics covered were discussed. In fact, the reporters in this office were more interested in knowing about India and the policies that are being formulated in the India currently.

XVI. Global Markets : Ms. Neale Steiniger

Ms. Neale Steiniger, gave an overview of the practices prevailing in the capital markets in other countries other than U.S.A. with specific reference to countries like United Kingdom, France, Germany, Australia and Switzerland. The various instruments, the method of pricing and the depository systems in these countries were discussed. The Euro Issues and Euro Markets were also covered and a model market was built considering all these factors.

XVII. Visit to Reuters

Reuters is in the process of installing System 3000, a system similar to that functioning at Bloomberg. An Introduction into the system and the way in which it functions was explained.

XVIII. Visit to the American Stock Exchange

At the American Stock Exchange, the visit was confined to the Stock Water. The system which sets off the alarm when excessive price rises or volumes are noticed was explained in detail. The steps taken by the department on noticing such an increase and the method in which it tracks down the persons behind creating such a market and the way in which the matter is referred to the SEC for further action was indicated.

XIX. Visit to the Securities and Exchange Commission : Mr. Robert Anthony

Mr. Robert Anthony, a lawyer and employee of the SEC. explained the way in which the SEC functions and the way in which the various cases before the SEC was investigated and action taken. The process of checking documents filed with the SEC at the time of the initial public offering , secondary offering and at regular intervals was also explained.

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XX. **Regulatory and operational problems facing foreign investors in India - Ms Julie Rogers and Ms. Jyoti Agarwala.**

The speakers were indicating the problems facing a foreign investors while he proposes to invest in India. Although some of the points raised relevant, most of the data presented was obsolete and total irrelevant in the light of the prevailing conditions in India. It is best that this lecture is avoided in the future sessions.

XXI. **Visit to the International Depository Corporation**

In this visit, the speakers were from the National Securities Clearing Corporation and the International Depository Corporation. The Speaker from the NSCC gave an insight to the history of the NSCC and the manner in which it functions. The impact of the Continuous Netting System (CNS) on clearing was also discussed in detail. The accounting/settlement procedure was also explained. The speaker from the international Depository Corporation explained the manner in which the U.S. markets moved into a scripless system. He also informed tha there were still ineligibles existing in the system. The manner which the dividends are distributed to the actual investors and the manner in which the physicals are stored were the other highlights of this lecture.

XXII. **Visit to the NASD**

The visit was to the NASD Regulators Inc., a new division of the NASD. The main function of this division is regulation, surveillance and compliance of all directives. A stock Watch is installed here which keeps an eye on the price and volume movement of the shares listed on the NASDAQ and the other market systems in the aegis of the NASDAQ. In case of an alarming rise in the prices of any scrip, the matter is immediately taken up by the NASD and investigated. The case is referred finally to the SEC for further action. The Regulatory aspect was discussed at length by four speakers, who give an overview with the various functions performed by each of the departments, they work in.

XXIII. **Visit to Merrill Lynch**

Merrill Lynch is the largest investment banker in the world and this visit emphasised on the regulatory procedures followed at Merrill. The session was divided into two parts, with the first session on Regulation and the second session on Compliance. The lecture was concentrated on the regulation of their employees, who might have access to price sensitive information and utilise the same for personal gains. The activities of all the broker

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employees are continuously monitored and the active accounts are reviewed monthly. In case, any lapses are noticed, the compliance wing immediately disciplines the employees. The trading, research and the investment bankers are separated and the regulatory practice is an ongoing process at Merrill with the employees also being continuously educated. They have a good relationship with the regulators also.

The training program was organised well by Baruch College (Mr. Bernard Lynch, Mr. Kishore Tandon and Mr. Peter Greenough). There was a good mixture of lectures and visits i.e., of theory and practical. It is very difficult to judge which of the lectures was the best, as all the speakers were good in their field and gave a thorough insight into the working of that particular aspect of the capital market. It is however felt, that the speakers of " the problems facing foreign investors in India" were not adequately prepared and presented data which pertained to the situation prevalent in India about 5 years ago. Apart from the classroom sessions, the arrangements were also made well. The group was received at the airport and were taken to the Hotel, the stay was comfortable and the group was also seen off at the Airport on the final day. On the whole, the training was informative and well-organised.

TRIP REPORT

" THE INDIAN SECURITIES AND EXCHANGE GROUP"

ARRANGED BY

BARUCH COLLEGE, THE CITY UNIVERSITY OF NEW YORK

FROM OCTOBER 28, 1996 TO NOVEMBER 15, 1996

(G.P. GARG)

(C.R. UNNY)

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INTRODUCTION

We were deputed to the captioned training programme at New York for a period of three weeks commencing from October 28, 1996. Apart from SEBI officials few participant were drawn from Stock Exchanges from Mumbai and Calcutta. The day to day schedule of programme, the list of institutions visited by us and officials with whom we were interacting as a part of the training is furnished in the Annexure. The day to day proceedings and our observations on the capital market scenario in US and other Emerging Markets are furnished below:

Oct. 28, 1996 :-

The day started with introduction in the Conference Centre of "Baruch College," The City University New York. Mr. Bernard Lynch introduced us with all the facilities available in the college and outside, during the training programme. He also took note of the type of speakers we would like to have and the places we would like to visit during the training programme. Since most of the participants were from SEBI and Stock Exchanges it emerged that understanding of U.S. Capital and Money Market with special emphasis on regulatory aspects would be a good idea. Prof. Kishore Tandon, thereafter, explained to us regarding the various speakers/ topic which were to be taken up during the training programme, and also included our suggestions regarding speakers we would like to have . It was felt that understanding of IPO's and filing of documents with SEC, USA would be helpful in knowing regulatory framework in USA vis-a-vis India.

In the afternoon, Prof. Tandon gave us an overall idea about the financial markets in U.S. Introduced us with the Glass Steagall Act of 1933. The act Separates" Commercial Banking" from "Investment Banking" though the distinction is slowly evaporating. The other issues were Role of underwriiters, Initial Public offerings, bounds and other money market instruments. The investment banks are mainly involved in issuing new corporate securities. The other important functions of investment bankers in U.S. are:

a) **Underwriting :-** Underwriting includes advising on terms and timing of offering, buying the securities from issued and distributing the issue to the public. The underwriter in addition to underwrite the issue by way of buying at the pre-set price and selling thereafter to public, may also agree only to use its expertise to sell the securities but does not buy the entire issue from issuer, which is known as best effort management. Also discussed other institutions such as Insurance Companies taking up life insurance, property and causality insurance.

b) **Investment Companies :-** These companies are very big and powerful in U.S., as they handle a lot of funds on behalf of investors investing in the form of mutual funds. Both open ended and closed ended funds were discussed. Other funds include aggressive growth, growth, growth income, precious metals, real estate mutual funds, global equity, sector specialised, high yield bonds. Municipal bond and index funds were also discussed. From Indian point of view real estate mutual funds, index funds if introduced in India, would be good.The index funds are managed by exchanges themselves, in which money is investment in proportion to the weighted average of the index. The assumption is that on the basis of past study only 20% funds are able to outperform index while the remaining are at par or below the growth of the index. Therefore, investment fund will grow in direct proportion to the growth of the index, if invested in index funds.

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Therefore, their returns will be more than the ordinary mutual funds. The concept of family of funds was also discussed, in which an investor can initially invest in a particular fund but has the option to switch over to the other funds in future based on his convenience and understanding regarding growth of the funds.

The pension funds were also discussed. The employees and employer contribute a fixed sum in the funds, which is subsequently invested in various instruments for proper growth of the funds, particularly in the stock market, so that the employees can get handsome return.

<u>Oct. 29, 1996:-</u>

The morning session was taken by Mr. Peter Greenough, M.D, Greenough & Co. Mr. Greenough was also the person co-ordinating our visits etc. with various market intermediators. He explained interlinks between various financial institutions and financial services providers. It became clear that private sector mutual funds play key role in the U.S. market. The investment by public is mainly made through the mutual funds which are managed by some key personnel. The various players of the market such as investor, broker, dealer, under writer, merchant bankers, stock exchanges, clearing corporations, depositing etc. were also discussed in brief. The role of regulators and media was also discussed.

The afternoon session was taken by Prof. Kishore Tandon. The issues discussed were U.S. exchanges and links between them. Role of SEC and SRO's etc.

Among the exchanges New York Stock Exchange (NYSE) is the biggest Stock Exchange of U.S where the equities of those companies having higher market capitalization and widely held by public are listed. AMEX (American Exchange) is the other stock exchange where those companies which are sufficiently large but not listed on NYSE are listed. Unlikely India, in U.S. a company can either be listed in NYSE or AMEX. The same cannot be listed on both the exchanges.

NASDAQ is over the counter exchange for smaller companies. There are some of the regional exchanges such as Chicago, San Francisco, etc. These exchanges are also linked with their counter parts such as NYSE or AMEX. To protect the interest of investors, all the trades are routed through specialists, so that an investor can get the advantage of the best price offer when he buys or sells securities. The stock exchanges in U.S. are self regulating organisation (SRO's) which are ultimately controlled by the Securities Exchange Commission (SEC) of U.S.A.

There was a brief discussion regarding SEC rule 144(A). Under the rule foreign companies can issue securities on private

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placement basis to the designated/ registered investment bankers. These securities can only be traded among these investment bankers, who can buy these securities for their various mutual funds etc. Therefore, indirectly the U.S. public is able to invest in these securities. The GDR market and premium on GDR's was also discussed. It emerged that premium on GDR's is because of their unregulated market, therefore, investors are not required to fulfil various requirements of Indian regulators. Moreover, they are freely tradeable providing investors an easy exit route.

Another important issue emerged was "Securities Asset Markets". The mortgage market is institutionalised in U.S: In this system, the people have option to take loan against mortgage of their property etc. These mortgages are subsequently purchased by specialised agencies such as FNMA, FHLMC, who provide the funds and manage the mortgages effectively. To raise such funds, these agencies issue securities in the market which are backed by the pool of mortgages. It has its own risks such as credit risk, liquidity risk, price risk etc. but overall this market is quite flourishing. This can perhaps be effectively utilized in Indian situation as well.

Oct. 30, 1996 :-

The entire day was dedicated to learn operation in the back office of a Broker's Office. The lecture was taken by Mr. Michael Curley. The discussion started from the opening of an account by a customer with the broker. There are rules specified by NASD indicating members to observe due diligence regarding the essential facts relating to its customers, accounts, orders that are handled by firm. Apart from general information about the customers, spouse, employer, etc. the investment objective is very important in U.S. This becomes necessary because brokers provide investment advice as well to their customers. All customers sign an agreement with the broker that they would handle the account within the exchange rules. Special care is taken for those customers who wants to participate in options due to their riskier nature. The type of account includes:

Cash Account :- The customer may purchase or sell any security in cash on carry basis, this is the most common account. As per Federal Reserve regulation 'T' of U.S, the payment or delivery must be promptly made but in no event later than 7 business day following the trade day. This is 2 day beyond the usual regular way settlement that broker require for each other, failing which broker will have to take prompt action to liquidate the position. This is to ensure that the counter party does not suffer. Also, the customer whose position is liquidate because of Reg. 'T' violation, his account will be 'blocked' or Frozen for 90 days. Further, a customer is not allowed the "free riding" using the sale proceeds of the sale of a security to pay for buying the same security.

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Margin Accounts :- Margin accounts are generally used for short sales and other sophisticated strategies prohibited in cash accounts. A customer having margin account must deposit half or more of the purchase price of any listed security and may borrow the remainder using the securities purchase as collateral. The other form is joint account passible for two or more individuals.

Advisory Account :- The customer signs a trading authorization or limited power of attorney which allows the advisor to make transactions without first consulting him or her. However, the advisor is expected to effect only those trades which are reasonably prudent and necessary to achieve the account's stated investment objectives.

The other things discussed include placing of orders by customers to buy or sell of securities, confirmations by broker which include information such as Trade date and time, settlement date, security, number of shares/ principal amount of bonds, Execution price, where executed, principal or agency transaction, commissions, accrued interest (for bonds only), net amount due inclusive of all fees etc.

Statements :- Rules of NYSE require that a statement of account be sent to each customer in any month in which the customer had any activity.

Lien Securities :- U.S laws allow that a broker has lien on a customer's securities for all commission, interest and advantages that may be due. In order to enforce lien, the broker may withhold delivery or if necessary may secure payment by selling the securities.

Commission :- As per SEC law, all commissions rates are negotiable.

Crossing Orders :- This is not allowed in the brokers office. A broker who receives equal size customer orders to buy or sell at the market (or receive a limit order within the current quotation) may act as agent for both sides by publicly offering and bidding the same number of shares within the current quotations.

From trading practice side, the issues discussed include kind of orders by customers, based on size of order (Round lot - odd lot), price limit (Market, Limit), Time limit (Day, week, month open), immediate or cancel, fill or kill, switch order, cash order, etc.

One of the very important issues discussed during the day was practice of "Short Selling". The short selling in the stock market is the practice of selling stock which seller does not own, for which delivery is to be effected by borrowing the shares.

The short sale is possible because a trader can borrow stock from the lender and then make a delivery of it. The stocks are generally borrowed from other clients of the same firm or from the other firms. Recently, institutional customers have become a major source of stock lenders for brokers. The lender has the advantage of receiving money in lieu of its stock as flat loan as generally no interest is payable and money so received can be utilized/ invested. Also, the lender gets the usual dividend/ rights etc. if any. The borrower gets money by short selling the stock. However, such transactions are marked to market on daily basis to protect the interest of both lender and short seller. A stock loan can be cancelled/ terminated by either party by a transaction notice.

For example, if a borrower borrows a stock flat, and sells at Rs.50/-, and covers the same in one month at 35 after decline of price. The transaction will be as follows:

Share Sales 100 Shares @ Rs.50/-		Rs.5,000.00
Selling Expenses:		
Commission :-	Rs. 100/-	
SEC Fee :-	Rs. 0.10/-	Rs. 100.10
(Rs. 1/- for each Rs.5,000/-)		
Net Proceeds		Rs.4,899.90
Add Margin @ 50%		Rs.2,449.95
Covering purchase 100 shares		Rs.7,349.85
@ Rs.35/-	Rs.3,500.00	
Commission (-) 70 +	70.07	Rs.3,570.07
SEC Fee		
		Rs.3,779.78
Deduct Margin Deposit		Rs.2,449.95
Net gain in Transaction		Rs.1,329.83

The role of specialist as market maker was also discussed in detail. Specialists are members of the exchange who engage in buying and selling of one or more specific issues of stock on the floor. The role is to maintain a free, continuous market in the securities in which they act as specialists. The specialist may act as broker or as dealer in transactions. As broker they execute orders for other brokers at a commission.

As dealer, they buy stock from public when it offer stock for sale but other public bids for purchase are not available and vice versa. The customers of the specialist are other members of exchanges. As specialists they do not transact business directly with the public. The Super DOT System (Designated Order Turnaround), facility allows expeditious execution of orders. A subscriber to DOT system may enter either a market or limit to the appropriate specialist post. These orders are thus exposed to auction market process. Thereafter, in most of the cases the orders are matched with each other, without specialist intervention.

Inter-market Trading System (ITS) :- To unify the stock exchange where same stock is traded, such markets have been linked with ITS. The system allows users to take advantage of favourable market orders for buy and sell.

Oct. 31, 1996 :-

The matter discussed during the day include Auditor's involvement with public company's filling with SEC and lecture was delivery by Mr. D. Edward Martin, CPA Partner, Richard A. Eisner & Co. The afternoon session was taken by Prof. Kishore Tandon and topic discussed was Investment banking process and security fillings. The initial discussion with Mr. Edward Martin was concentrated on filing of prospectus with SEC for the issue of equity shares to general public. It was found generally in line with similar process being followed by SEBI in India. The accounts or all financial statements are prepared by auditors on the basis of Generally Accepted Accounting Standard (GAAS) of U.S. The prospectus summary includes Risk Factors, use of proceeds, Dilution, Capitalization, Dividend Policy, Selected Financial Data, Management's decision and analysis, Business, Managements, Principal Stockholders, Selling Security Holders, Description of Securities, Underwriting, Legal matters, Experts, Available information, Index to financial statements and finally the Independent Auditor's Report (IAR). The IAR is very important as it indicates auditors perception about companies' earning prospects in future and its capability in meeting the earning projections.

Next topic discussed was filing of Form 10-K with SEC, U.S. Form 10-K is the Annual Report of the company in pursuant to Section 13 or 15 (d) of Securities And Exchange Act of 1934. This is very detailed report indicating all the important development took place during the last one year in the company. Another filing discussed was form 10-Q. This is quarterly report to be submitted by companies with SEC in pursuant to Section 13 or 15 (d) of the SEC Act 1934. It is in two parts. Part I contains Financial Information such as Consolidated Balance Sheet, Statement of Operation of last 3 and 6 months, Cash Flow Statements, Management discussions and analysis of financial condition of the company. The Part II contains other general information about the company.

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Nov. 01, 1996 :-

The morning session was dedicated to clearing issues in derivative markets. It was a very important lecture from Prof. Terry Martell. It started with future contracts, which is an agreement to buy or sell a commodity sometime in future with the price determined today. A well developed commodity future markets could be very helpful for a country like India, where a large population still depends on Agriculture.

Future markets provide a unique mechanism for transfer of risks from hedgers representing commercial interests, to outside investors. Hedging enables growers, producers, merchants, processors and manufacturers to reduce their price risk exposure in the cash market by taking equal and opposite position in future markets. Future markets are not designated to act as a substitute for the actual sale or purchase of a commodity, but act as a form of forward pricing.

A futures option is the right, but not the obligation, to buy or sell a specific futures contract at a given price on or before a stipulated date. If the option buyer does not exercise the right during the specified time, the option expires. There are two types of options: calls and puts. Call options give the purchaser the right to buy the underlying futures contract at a particular price, known as the striking price, any time between the purchase date and the expiration of the option. Put options give the purchaser the right to sell the underlying futures contract at a specified striking price any time between the purchase date and the expiration of the option.

Hedgers are commercial firms who trade futures and options to reduce their exposure to price risk in the cash market. Hedging with futures and options can enhance a firm's profit performance and assist in business planning. Several large multinational corporations are members of the Exchange, and many others use the markets daily.

The trading in futures and options is carried out in Coffee Sugar and Cocoa Exchange Inc. (CSEC). CSEC is regulated by the commodity futures trading commission (CFTC) of US.

The afternoon session was taken by Mr. Juan Pujol. The matters discussed include Private placement of equity, leverage buyouts, management hybrid and capital restructuring.

Due to various complications involved relating to regulations, around 10% to 15% of total capital raised is carried out through private placement of the equity. This area is becoming more and more popular because of a lot of regulations and expenses involved in issuing the equity to the public. Moreover the corporate feels that by issuing equity on select basis they are able to concentrate more on their business and it allows them better performance.

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The private equity placement is only on the basis of negotiation between the parties concerned. The firms specialised in placement of private equity plays pivotal role in analysing the rate, and percentage of equity to be issued on private basis. This is also done for capital restructuring and management buyouts as well.

Nov 4, 1996

The morning session was dedicated for learning the working of New York Stock Exchange and other related issues. The lecture was delivered by Mr. David Krell, Vice President of NYSE.

Apart from other matters, the trading execution, role of specialist, super dot system, ITS were discussed in detail. NYSE is a hybrid exchange with call auction in the beginning, continuous auction post opening with some dealer participation. The orders are executed with or without intervention of specialist. Also they are automatic as well as based on auction.

For listing on NYSE for US companies the minimum standards to be followed are as follows:

Share holders	2000
Public shares (million)	1.1
Market value ($ million)	40

As on 30, April, 1996, the total companies listed with NYSE were 2,710 out of which 248 were non US companies.

Shri. Krell also explained internat trading system which is an electronic connection network, links participating US exchanges, OTC market and facilitates the execution at the BEST ITS quote.

There are at present 1366 membership seats. The number has been unchanged since 1953. NYSE is governed by the Board of Directors, 12 Securities Industry Directors, 12 Public Directors, 2 Full time Officers (Chairman and Vice President) who are paid by NYSE. The main source of revenue includes listing fees, trading fees and market data fees. There is system of an specialist in NYSE they have been assigned with one stock. Specialists acts as brokers arranging trade, Occasionally act as dealers. specialist revenues include commissions, trading (spread and market). specialist obligation include continuously post prices at which investors can trade manage the order flow and stabilises prices.

In the afternoon we visited the Bloomerberg Business News at Park Ave, New York.

Bloomberg is a private business channel and it is growing very fast as they have provided approx. 70,000 terminal in USA providing business news pertaining to large numbers of companies.

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Even their business news are used by the stock exchanges, regulators etc. They provide news about 20,000 companies on online basis which are from USA, Germany, India, England, Korea, Japan etc. The channel also provides news about current affairs,

politics, games etc. The channel also provides analysis about trading volume in different stocks. Their price movement etc., also provides the data about stock, companies performance during last 10 years. The on line information by Bloomberg can be very useful for regulators as they also provide latest news about companies trading volume, price movement etc. We subsequently revealed that the Surveillance Department of AMEX was using Bloomberg Business News channel for the Surveillance.

<u>Nov 5, 1996</u>

The morning session was taken by Mr. Phillip Zweig from Business Week, formerly at the Wall Street Journal and Corporate Finance, author of various books. Mr. Phillip is a freelance journalist. We had a very free and frank discussions regarding role of regulator and press to create public awareness about capital market. The role of press in detecting fraud and unathecal practises was also discussed. Their was consensun of the view that congenial relationship between press and regulator with mutual respect for each other can be very helpful for dissemination of information to the public etc.

The afternoon session was for the visit to Fedral Reserve Bank of New York. The visit was not very relevant to the course, However, we came to learn about the role of Fedral Reserve Bank of New York which is totally independent in their working like Reserve Bank of India. It also acts independently for the control of inflammation and growth of economy of USA. We also saw the Gold Reserve etc. being maintained by various countries with the Federal Reserve Bank of New York

<u>Nov 6, 1996</u>

In the morning we visited UZB Partners. They are maintaining Hedge Funds on behalf of their selected group of investors. Hedge Fund are high growth funds. Accordingly, they are risky as well from the investors point of view. However, these fund are popular among young and enterprising investors who wants high growth to their fund.

The Fund management have minimum bench mark to charge their fees for eg. If the minimum bench mark in 20% of the growth, no fee will be payable to the fund management if the fund growth during the year is less than 20%. Also, if the fund management is not able to perform during the particular year, they have to offset the deficit in performance during the next year to earn their fee. The funds Manager expressed some of their concern about strict regulators frame work in India and requested for more liberalisation. However, they were not very specific when we asked the areas where they want more liberalisation in India.

Thereafter, we visited Securities Industry Automation Corporation (SIAC) and the group was addressed by Mr. Neal Quinn. The SIAC is basically handling those securities which are not paper less. Therefore physical delivery of document/securities is involved. The system adopted by SIAC is quite sophisticated and efficient to ensure that transfer of securities from one broker dealer to another broker dealer takes place on prompt basis.

In the afternoon we visited Nomura Securities . The main speaker was Mrs. Linda Quinn, former chief of the division of Corporate Finance at the SEC. The discussion was regarding corporate finance from a regulatory prospective . Also various issues involved in the securities trading were discussed. The various matter involved in filing of IPOs, selling of securities to public etc. were discussed during the meeting.

Nov 7, 1996

In the morning we visited Coffee Sugar and Cocoa Exchange (CSCE) at the World Trade Centre, New York. It was a very good experience as we were able to see the actual trading at the time of opening of the CSCE. We also had the discussion with the Marketing Executive of the CSCE. Prof. Terry Martell who had earlier delivered a lecture on November 1, 1996 in this regard were also present. The various issues involved in clearing, prices, margin and surveillance of the market were discussed. The CSCE has a strong surveillance and complain mechanism which monitor not only the trading activities but also financial conditions of members.

To maintain orderly markets and percent excessive speculation, the exchange continuously montior the position of large trading firms. The compliance activities of the exchange includes monitoring of floor trading practices, high on-site surveillance, sophisticate computer, review of members records and analysis of trading data compiled through the clearing process.

The Commodity Futures Clearing Corporation of New York (CFCCNY) clears every matched trade on the CSCE and assumes the role of counterparty. By interposing itself between buyers and sellers, CFCCNY becomes the issuer and obligor of all contracts traded on the exchange, a function which services as a crucial guarantee of contract performance. Clearing members are required to meet stringent financial requirements which dictate the size of the positions they may carry.

To guarantee contract performance, the Exchange requires that market participants make original and variation margin payments.

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Original margins are "good faith deposits" established to ensure market participants will meet their contractual financial obligations. Original margins are constantly monitored by the exchange and are periodically adjusted to reflect changing market conditions such as increased price volatility. At the close of each trading day, margin accounts are "marked to the market": adjusted to reflect price movements in the futures market. When prices move unfavourable to a trader's positions, additional or variation margin payments are required to restore margin to original levels.

In the afternoon we visited Securities Training Corporation (STC). It is stated that as per US laws all people involved in securities training etc. have to pass required examination before they can actually engage them in the business. Therefore there is different level of exams to be passed by individuals before they can transact the business. STC provide training to the individuals or staff of various firms dealing in securities. After passing the exam the person gets a certificate and thereafter require to start the business within two years during which the certificate is valid.

During the discussion we also came to learn about the Central Registration Depositories (CRD). All the person involved in securities matters such as broker, dealer, merchant banks are required to keep record of all their personal on CRD. The CRD up dates record of each individual on the basis of their conduct, market news, their employer report etc. These information are available to public at large so that the public has sufficient information about their individuals to whom they are interested to conduct their business. It helps investor so that they are well aware about the individual brokers, firms to whom they are transacting the business. Further the system to providing licence to the individuals involved in securities business has also improved the quality of the business and the people are better and chances of errors are less. It is expected that people who have sufficient knowledge in the securities market will be able to serve better as compared to person who is not conversant with this system.

In the evening we visited the weekly named Emerging Markets week and had discussion with the reporters conveying various emerging markets. Incidentally, Indian market is covered by their Hong Kong office. Therefore, they were not able to discuss much about the subject. We had brief idea regarding trading practises the other emerging markets such as Mexico and Brazil. It is felt that the present state of Indian markets and the latest development such as screen based trading, depository system etc, are not widely known to the US investors.

November 08, 1996

The lecture was delivered by Ms. Neale Steniger of Nene Schaffen & Co., regarding global securities market, trades execution,

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clearance of settlements procedures. The initial discussion was about the type of system prevailing in United States, UK, Germany, Brazil, Japan, Peru, India etc. It was felt that in most of the markets the Stock Exchanges functioning is computerised. However, while some of the markets had the system of specialist form the other markets had the system of market makers.

The various steps of market and trading practices, regarding new issues were discussed which include the issuing of securities to the public. The process includes negotiations Vs. competition, local and global, issues valuation etc. Subscription/ application, book building, firm commitment etc. was discussed. The matters relating to under writers, agreements were also discussed during the session. the session also included the discussion regarding market and trading practices relating to the secondary market. The system prevailing at various places, such as order driven and price driven markets.

Order Driven

Roll Call:

Securities are alphabetically called, at a designated time, during the day. All orders matched with the other side are executed.

Price Fix:

One execution price is computed and all orders for that day are executed at that price. The price is based on the average of all orders received by the time of fixing.

Continuous Trading:

Securities are continuously traded during market hours. Orders are either executed on the floor by brokers via the 'open outcry' method or input and matched in a computer system.

Specialist:

Stock Exchange designates one broker to whom orders are directed and will maintain a quote in a security.

Alternative Trading (matching) Systems:

Orders entered by institutions and broker/ dealers as indications of interest or to be matched and executed.

The matters relating to American Depository Receipts (ADRs) were also discussed which included public offering relating to level 1, level 2, level 3 of the ADRs. The matters relating to GDRs were actively discussed. The discussions also included efforts

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being made by various Stock Exchanges to improve regulatory over sight and increase investors protection.

The European Union Directive for this include access to an investors to any of the exchanges. Therefore, the exchanges should be inter connected to provide the best price to the investors. The other measures include transparency in the transactions, rules to conduct for the above places, and investors protection fund. The measures being taken by Stock Exchanges to stop insider trading, reports regarding substantial holding were discussed. There was also discussion on the International Securities Market Association (ISMA) which gives recommendations regarding trading, settlement, disciplinary personates, projects taken up by the parties.

The role of group 30 which is a consortium of 30 big Stock Exchanges to give their recommendations regarding improvement of trading practices were also discussed. The group 30 has already given 9 recommendations for improvement. The discussion regarding physical delivery of the securities as well as the central depository system and immobilisation of the securities were also discussed.

It was felt that the central Depository system is better which leads to scrip less trading. It should be supported by the screen based trading in the Stock Exchanges with an efficient clearance with electronic transfer of the funds by the banks.

There was also discussion about measures to be taken for creating equity culture in the general public. It was felt that the Government should initially offer the shares of profit making Public Sector Units (PSU) at discounted price thereafter, the management of the PSU should be given free hand so that the PSU can perform and the shareholders have rich harvests on their investments. It would boost the market sentiments, and motivate the public to invest in the equity.

It was felt that the country like Germany, where people have not shown much enthusiasm about investment in shares, their Government has resorted to such practices. The German Telecom Issues in the market was discussed by the participants in this context.

The afternoon session was dedicated to discussing the ideal market for trading practices. It was felt that the market should have a screen based trading, with the provision of depository so that a scrip less trading system can be implemented. It was also felt that there should be mechanism of electronic transfer of funds for quick pay-in and pay-out on settlement dates. It was further observed, that the computers will play vital role in checking the mal- practices relating to Stock Markets.

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It was also felt that in the future date if the major Stock Exchanges can be connected globally, there will be sea change in the trading practices and uniformity will come in the market.

Nov 11,1996

It started with the visit of office of Reuters. The Reuters has developed system 3000 pertaining to securities market. The system can be provided world vide to their subscriber on certain payment.

This is a very comprehensive system with on line information of about 20000 companies world over. The system has the record of annual performance of the companies during the last 10 years as well as data regarding trading in the equity of the companies.

The system can also provide various ratio analysis to facilitate investor to have an idea of various financial parameters of the companies concerned. The system can also provide trading volume, price movements etc. on daily basis, which can be very helpful from the surveillance point of view, to have a price and volume movements of various securities.

The next visit of the group was to American Stock Exchange (AMEX) with particular reference to Surveillance Department. The presentation was given by Mr. Jay Bono an official of AMEX. The discussion was regarding market surveillance, practises followed by AMEX. Mr. Bono explained how they watch unusual movement in the prices of any scrips, as and when the price crosses the certain break limit fixed by them, they start investigating the matter. He also explained that they keep strict control about unusual volume in particular scrip.

Mr. Bono also explained that the system 3000 developed by Ruters and the Bloomberg system is very helpful in their day to day functioning. Whenever they see unusual movements in the particular scrip the matter is discussed by them with all parties concerned including company management to know the reasons for ususal movements in the price or volume of the scrip.

The matter is investigated by them and they have the right to stop the trading in the scrip temporarily to avoid complications in future.

AMEX also investigate matters regarding insider trading for which they also rely on the information being disseminated by various news agencies, financial dailies, magazines etc. He explained that the software developed by them is confidential in nature which they have created, based on their past experiences. He also explained their mechanism for prosecution of erring persons

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by way of prosecuting them through Securities Exchange commission and office of attorney. During the discussion it was also learnt that there were instances where their system can give false warnings. Therefore, they are very careful while initiating proceeding against any company, individual etc.

In the afternoon, the group had the chance to visit New York Stock Exchange (NYSE) and the presentation were given by their officials of surveillance and operation departments followed by visit of the group members to watch the actual working of NYSE. NYSE is one of the biggest securities market in the world. At present there are around 2710 companies who have listed their share on the NYSE. These companies are from various countries all over the world. The initial discussion was regarding measures taken by NYSE to enforce various regulations. It was explained by NYSE officials that what ever regulations prescribed by them are strictly adhered to and there is no exemption. NYSE had its own mechanism to stop the practise of insider trading. The discussion was regarding the role of specialist in providing two way quotes to ensure stability as well as liquidity in the market. It was learnt that specialist acting as either buyer or seller in 17.5 % of the share volume traded in 1995. Therefore, the remaining 82.8% of the 1995 share volume resulting from public and member firm orders meeting directly in NYSE market.

NYSE has its own system to avoid volatility in the stock market. As per rule 80 A when the Dow Jones Industrial Average (DJIA) moves 50 point or more from the previous days close, the above rule applies. Accordingly, in down market share orders may be only on a plus or zero plus tick while in up market order may be executed only on a minus or zero minus tick. The rule applies for the remaining days, unless the DJIA moves back within 25 points of the previous days close.

As per the rule 80 B when DJIA decline 250 points from the previous days close the trading is halted for one hour while the trading is halted for two hours, in case of DJIA declines 400 points or more from the previous days close.

Another system of NYSE to provide proper information to the investors is that the all trade executed must be displayed on the system.

Another mechanism to ensure efficiency in the market and investor protection is based on Intermarket Trading System (ITS). ITS is an electronic communication network which links nine markets. New York, American, Boston, Chicago, Cincinati, Pacific and Philedelphia stock exchanges, the Chicago options exchange and the NASD. The system enables market professionals to interact with their counter parts in their markets whenever the nation wide consolidation quotation system shows a before price.

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During the discussion the NYSE officials informed that due to their strict listing requirements and efficient market practices there is substantial growth in market capitalization of the stocks listed on NYSE. The NYSE is making serious efforts to attract more stock for listing on NYSE. NYSE officials explained the criteria for listing of non US corporation which is as follows.

New York Stock Exchange Listing Standards:

Non-US corporations may elect to qualify for listing under either the alternative listing standards for non-US corporation or the NYSE's domestic listing criteria. However, an applicant company must meet all the criteria within the standards under which it seeks to qualify for listing.

Alternate Listing Standards:

The alternate listing standards are designed to enable major non-U.S. corporations to list their shares on the New York Stock Exchange. The principal criteria focus on worldwide rather that U.S. distribution of an overseas company's shares and apply wherethere is a broad, liquid market for a company's shares in its country of origin.

Shareholders

Round-lot-holders (holders of a unit of trading -- generally 100 shares)	5,000 worldwide
Public shares	2,500,000 worldwide
Market Value of Public shares	$100,000,000 worldwide
Net tangible Assets	$100,000000
Demonstrated earning power over three years	
Aggregate for the three years Pre-tax income	$100,000,000
Minimum in any one of the three years	$25,000,000

Sponsorship by NYSE member firm

Because of the widespread use of bearer shares outside the United States, some non-U.S. corporations might have difficulty in demonstrating that they have the required numbers of shareholders on a worldwide basis. In such cases, sponsorship by a New York Stock Exchange member firm as to the liquidity and depth of the market for a company's shares may substitute for documentation concerning the number of shareholders.

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Domestic Listing Standards

Domestic listing requirements call for minimum distribution of company's shares within the United States. Distribution of shares can be attained through U.S. public offerings, acquisition made in the U.S. or by other similar means. Note that there are alternatives to the round lot-holder and demonstrated earning power standards.

Original Listing Standards:

Shareholders (A,B)

Shareholders (A, B) Round-lot Holders (holders of a unit of trading--generally 100 shares)	2,000 U.S.
or:	
Total Shareholders	2,200 U.S.
and average monthly trading volume (for the most recent six months)	100,000 shares U.S.
Total Shareholders	500 U.S.
and average monthly trading volume (for the most recent twelve months)	100,000 shares U.S.
Public shares (B)	1,100,000 U.S.
Market Value of Public Shares (B,C)	$40,000,000 U.S.
Net tangible Assets (D)	$40,000000
Demonstrated Earning Power Over Three Years	
Most recent Year Pe-tax Income	$2,500,000
Each of Tow Preceding Years Pre-Tax Income	$2,000,000
or:	
Aggregate for the three years Pre-Tax Income	$6,500,000
Minimum in the most recent year (all three years must be profitable)	$4,500,000

We had the occasion of watching actual trading on NYSE floor.

November 12, 1996

In the morning session we visited office of securities and exchange commission (SEC), there was general discussion regarding investor protection and growth of capital market in USA. There

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was brief discussion regarding Glass-Steagell Act 1933 (GSA). The SEC is an independent agency of Ferdral Government headed by five members appointed by the President and approved by majority vote of the Senate. The commission exercises not only executive but also judicial powers. The commission is relatively independent because the SEC commissioner can only be removed for mis conduct. Also the commissioners are appointed for staggered term of five years. As per the SEC rules, no more than three commissioner can be members of the same political party. As per the federal law some of the commissions meeting are open to the public. There was general discussion regarding SEC rule and Mr. Robert Anthony explained that SEC believes in the concept of Self Regulating organisation (SRO). Also, the full disclosures about various issues relating to issue of securities in the market so that investors can make proper judgement of their own. The US Government has given sweeping powers to SEC to take care of investor protection. There are large number of cases in the SEC is a party. SEC can also initiate prosecution against erring companies at their own or with the help of the office of attorney. There was also discussions regarding enforcement procedure and being followed by GSE.

In the afternoon we had discussion with Ms. Julie Rogers and Jyoti Agarwala regarding regulatory and problems being faced by foreign investors in India. It is felt that US investors in general are not familiar with market practises in India. Initially, they expressed their apprehension about delay in FII registration by SEBI and we explained to them that the things have totally changed and there is hardly any case pending for FII registration. They expressed their fear regarding over regulations and inefficiency in Indian system. However, their information on some of the matters were not correct for eg. Delay in transfer of shares, non payment of dividend by the company. They also expressed apprehension regarding dispute resolving mechanism by Stock Exchange in the country.

They also expressed their apprehension regarding problem being faced by the FIIs due to long time in transfer of shares as well as non transfer of shares on flimsy grounds. They also indicated that the clearing system is very poor in the country and there is a backlog of 3 to 6 years in reconciliation of Bank's accounts. Some of their observations seem to be exaggerated. They were informed by us that with the NSE and BSE going for screen based trading and other Stock Exchanges following the same, most of the trading in India would be screen based. Also, with the depository system in the country taking place, the country is going for full modernisation of the trading practices.

November 13, 1996

In the morning, we had discussion in the office of International Depository Corporation. The depository is one of the biggest

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depository in the world with an advanced computer system for the purpose of efficiency in the system.

We also had discussed with the officials of NSCC i.e., National Securities Clearing Corporation. The rule of NSCC is to ensure cost effective system for trading processing clearance, delivery and settlements. NSCC is owned by NYSC, AMEX, NASD etc. NSCC act as a counterparty to guarantee all trades taking place on the Stock Exchanges. In the afternoon, we visited the office of National Association of Securities Dealers (NASD). NASD is a self-regulatory organization responsible for the regulation of The Nasdaq, as well as the over-the-counter securities market.

The NASD carries out its regulatory responsibilities through member education; on-site examinations of member firms to determine their compliance with federal securities laws and NASD rules and regulations; continuous automated surveillance of the markets it operates; the registration and testing of securities professionals; the review off member's advertising and sales literature; the review of underwriting arrangements proposed by members in connection with new offerings of securities; cooperative programs with government agencies and industry organizations to solve problems affecting investors, public companies, and member firms; and forums for investors and members to arbitrate disputes.

Market Surveillance

While the NASD's broker/ dealer regulatory programs are carried out in 14 district offices throughout the country, surveillance of The Nasdaq Stock Market is centralized in the Market Surveillance Department.

The Market Surveillance staff is aided by a variety of automated systems that analyze trading activity on a monthly, weekly, and daily basis.

Among these is the Stock Watch Automatic Tracking (SWAT) system, which employs a number of sophisticated statistical models and parameters to alert Market Surveillance analysts to any unusual price or volume movements in any Nasdaq security.

The SWAT system also captures news on-line, allowing Stock Watch calculations to include news as a criterion for unusual price or volume movement. An incident tracking function links the Stock Watch parameter breaks with related news stories, captures information on the analysis performed for each alert, and provides an historical reference on all alerts.

The Nasdaq Equity Audit Trail provides a fully integrated data base of second-by-second quotation, transaction, and clearing

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detail for all Nasdaq securities on a firm-by-firm basis. This historical record of trading in Nasdaq securities is used in a broad range of NASD surveillance systems and provides an efficient and effective means of overseeing trading activity in the Nasdaq market.

These sophisticated tools enable Market Surveillance analysts to reconstruct unusual trading patterns and create a complete audit trail of quotation changes by all market makers in an issue. These capabilities facilitate the efforts of analysts to investigate insider-trading cases and document other instances of questionable activity.

Market Surveillance will often impose trading halts to permit the dissemination by an issuer of material news to market participants. Once the news is widely distributed over a major wire service to investors, trading is resumed.

November 14, 1996

In the morning, we visited the office of Merrill Lynch and had discussion with their officials from compliance department. The emphasis of Merrill Lynch was that they work for the best of the interest of the market and their customers. Also, they fulfil all the obligations regarding their duties to comply with various SEC rules as well as the federal law.

In the afternoon, we visited the Baruch College Library/ Computer Centre to see SEC Edgar Filings. It is found that all the information relating to SEC are available on inter-net and all the documents relating to IPOs are made available by SEC to the public through SEC Edgar Filings system. This helps investors in knowing all details about the companies, they intended to buy their equities etc.

The last day of the programme i.e. November 15, 1996 was regarding investment banking and open questions from the group regarding the total visit. It was followed by Luncheon/ Reception and Presentation of Certificates.

CONCLUSION

To sum up the training programme of "The Indian Securities and Exchange Group" arranged by Baruch College for the period of three week w.e.f. October 28, 1996 was well structured and we had a good exposure of the US Capital Market and other Emerging markets in the world. Though some of the speakers were very eminent in the respective field, they were found to be not fully conversant with certain practices and procedures prevailing in Indian capital market system. This was instrumental in having certain gap between the trainees and trainers. It is suggested that these speakers who are well conversant with US capital market procedures may be invited to India for imparting training programme to the Officers of SEBI and various intermediaries etc. The speaker, so invited, can avail of this opportunity by to have a first hand knowledge of procedure obtaining in Indian capital market system so that they can be more effective compared to the system prevailing in Indian capital market and other emerging capital markets in the world.

The other logistic arrangement made by the authorities in New York were found to be good and the participant were well taken care of at every stage by the co-ordinators especially Mr. Bernard. In short, the pilot training programme conducted by Baruch College in collaboration with USAID authorities is an experiment worth continuing so that more Officers of SEBI/other self regulatory organisation could be exposed to capital market scenario in other countries.

ANNEXURE

Indian Securities and Exchange Group

November, 1996

Week 1:

Monday, Oct. 28:	Mr. Bernard Lynch, Manager, School of Business & Kishore Tandon, Professor of Finance, Baruch College, The City of New York	Orientation & Introduction Introduction to U.S. money & capital markets and institutions
Tuesday, Oct 29:	Mr. Peter Greennough, Managing Directors, Greennough & Company Inc.	Interlinks between relevant financial institutions and financial-services providers, etc
	Prof. Kishore Tandon	U.S. exchanges and links between them; Role of SEC, CFTC, OCC
Wednesday, Oct. 30:	Mr. Michael Curley	Brokerage Operations: All back office operations
Thursday, Oct. 31:	Mr. Ed Martin, CPA Partner with a leading auditing firm	Auditor's involvement with public company's filings with SEC
	Prof. Kishore Tandon	Investment banking process and security filings
Friday, Nov. 1:	Prof. Terry Martell Ph.D. The Weissman Centre, for International Business	Clearing issues in derivative markets
	Mr. Juan Pujol	Private equity area including leverage buyouts, management buyouts, and capital restructuring

Week 2:

Monday, Nov. 4:	Mr. David Krell, Vice President (Operation), NYSE, New York	Working of NYSE & links with regional exchanges: Auction vs. dealer market
	Mr. Peter Greenough	Visit to Bloomberg Business News

Tuesday, Nov 5:	Mr. Phillip Zweig, Department Editor Business Week- New York	Formerly at the Wall Street Journal and Corporate Finance, author of various books
	Mr.Kishore Tandon and and Bernard Lynch	Visit to Federal Reserve Bank of New York
Wednesday, Nov 6:	Mr. Vishhal Garg VZB Partners, L.L.C.	Visit to VZB Partners (Hedge Fund)
	Mr. Neal Quinn	Visit to SIAC (Securities Industry Automation Corporation)
	Ms. Linda Quinn and Mr. Danielle Carbone	Visit to Normura Securities Discussion on corporate finance: from regulatory perspective
Thursday, Nov. 7:	Mr. Terrence F. Martell	Visit to Coffee Cocoa Sugar Exchange
	Mr. Todd B. Rosefeld Executive Vice President, Securities Training Corp., New York	Securities Industry registration, CRD (Central Registration Depository), and Licensing exams
	Mr. Aaron.W. Finkel, Managing Director, Emerging Markets Week	Emerging Markets Week/ Institutional Investor Magazine
Friday, Nov. 8:	Ms. Neale Steinger Management Consultant Nene Schaffen & Company	Global trade execution, clearance, settlement and custody

Week 3:

Monday, Nov. 11:	Mr. Peter Greenough	Visit to Reuters -To view System 3000
	Mr. Jay Bono, Officer, Market Surveillance Department, AMEX.	Visit to American Stock Exchange
	Mr. David Krell, Vice President, NYSE.	Visit to the New York Stock Exchange
Tuesday, Nov. 12:	Mr. Robert Anthony, Officer, SEC, New York	Visit to the Securities and Exchange Commission
	Ms.Julie Rogers M.B.A & Ms. Jyoti Aggrawala, M.B.A.	Regulatory and operational problems facing foreign investors in India

Wednesday, Nov. 13:	Mr. Cecilia Humphrey, Manager & Mr. Edward J. Mc.Guire, Jr. Secretary, The Deposit Trust Company	Visit to IDC (International Depository Corporation)
	-	Visit to NASD
Thursday, Nov. 14:	-	Visit to Merrill Lynch
	Prof. Diane DiMartino	Baruch College library/ Computer Centre: SEC Edgar Filings
Friday, Nov. 15:	Prof. Kishore Tandon	Investment Banking, and open questions from group regarding total visit
	-	Luncheon Reception and Presentation of Certificates

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APPENDIX G

PW critique of project performance indicators

Price Waterhouse LLP

MEMORANDUM

TO	:	**Mr. Peter Thorman, USAID**
FRM	:	**Dennis Grubb**
CC	:	**Mr. Alan Roth/Mr. R. Diehl**
DTD	:	**January 21, 1997**
SUB	:	**Program Performance Monitoring Plan**

Based on our discussions of today's date we draw your attention to our concerns on the data presented in the USAID Program Performance Monitoring Plan , India. We understand the evaluation team (Messrs Roth and Diehl) will make suggestions on developing the improved Program Performance Monitoring Plan.

For your information please find enclosed our memorandum prepared in 1996 on the inconsistencies and shortcomings of the current TCS baseline model. We had forwarded the memorandum to USAID, Delhi during the preparation of the Performance Plan for 1996.

Best regards,

Inconsistencies and shortcomings of the TCS baseline model

1. We have tried to update the TCS model based on the data sources specified by them and have at times comes across data that is inconsistent with what they have specified in their model.

2. On the issue of the number of investors in the capital markets, we have been unable to check the figure given by TCS. We could not get a reliable figure either from the sources specified by them or from any other source.

3. The sources specified by TCS are annual sources and, also, the reports published by these sources often come out several months after the end of the financial year and this makes the task of regular updation difficult. We would prefer to use CMIE data as this is published every month and is also considered very reliable.

4. We also have reservations about the criteria that TCS has used for measuring the progress of the Indian markets in terms of structural improvements. The criteria tend to measure the economic success of India more than the reform and expansion of the capital markets. Details of this are given in the attached sheets.

5. The TCS model is also fundamentally flawed. E.g., they have budgeted the introduction of options trading before that of futures when options, being options on futures, cannot be introduced in the absence of futures contracts.

Memo	To :	USAID/Program Office
	From :	PW-OGS/FIRE

Analysis of the baseline model by TCS and suggestions for improvements

Strategic objective 1.1: Increased amount of new capital (equity and debt) raised through the securities market (Rs. Billion)

Data Sources used: SEBI Annual Report

Other sources available: CMIE monthly reports on the Indian economy. This gives the amount raised through each new issue in that month and also gives the issues expected in the near future. The advantage over the SEBI report is that it gives the data each month instead of each year.

The RBI annual report can be used as an additional source of data because it gives the total disbursements of the banking system and financial institutions. It also gives the net investment of financial institutions (including UTI, GIC & LIC) and banks in securitised debt and equity and is hence an indicator of the institutionalization of investment and hence a greater maturity in the markets.

Stock exchange statistics should be used to compare the increase in the capitalization through new issues on the individual exchanges. A shift towards the NSE and OTCEI would indicate a change in the promoter profile towards greater transparency.

Comments: An increase in the volume of issues is also a function of the macroeconomic environment in terms of money supply and government spending and also the credit policy of the RBI. Thus, it makes sense to factor these into the model. A possible solution lies in monitoring the ratio of securitised capital and loan disbursements for investment financing. Any improvement in this ratio would indicate a greater maturity in the capital markets.

Also, if the CMIE monthly reports are used then the three-month moving average can be used to update the data every month and hence areas for improvement can be identified faster.

Also, the strategic objective talks only of the increase in IPOs. The strategic objective given to us (FIRE) included secondary market activity. Thus, while the breadth of the markets has

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been measured, the depth in the market in terms of volume of secondary market activity has not been addressed.

Possible solutions lie in recording the three-month moving average of the daily turnover on the NSE and the BSE as far as the equity markets go. Also, since any change in trading activity could also be a result of macroeconomic factors it makes sense to also measure the ratio of the volumes against the volatility in the stock market indices. If the volumes increase while the volatility does not increase that much it would be an indication of greater depth in the market.

In the case of the debt markets the same procedure could be followed and also the activity on the NSE should be compared to the activity in the telephone market (the source of data would be the SGL accounts with the RBI). Any increase in this ratio would indicate that the market is shifting from a telephone market controlled by a few players to a more transparent system.

There are no indicators for the progress of the money market. The development of the money market is essential as it drives the longer end of the market. A possible indicator could be the volatility in the call money rates over a period of three months. A stable call would also help promote a term money market which could then be used as a benchmark for floating rate notes. The volatility in the call is also a result macroeconomic factors, specifically, the government's borrowing programme and the monetary policy pursued by the RBI and hence this may not be a totally accurate indicator of the development of the money market. Some thinking has to be done on this account.

Strategic objective 1.2: Increased foreign indirect institutional (portfolio) investment

Data sources used: SEBI Annual Report

Other sources available: CMIE monthly reports on the Indian economy. This gives the amount raised through each new issue in that month and also gives the issues expected in the near future. The advantage over the SEBI report is that it gives the data each month instead of each year.

Comments: The FII investments are not only a function of the Indian macroeconomic environment but are also influenced by global interest rates and stock markets, e.g., increases in US interest rates

or the recent boom of the Dow Jones Index have the effect of sucking money away from emerging markets.
FII investments in India also compete with investments in other emerging markets as most fund managers tend to limit their total exposure to emerging markets.

A possible solution is to compare FII activity in India with the activity in Indian GDRs and ECBs for both secondary market trading and IPOs. A shift toward direct investment in the financial markets as opposed to GDRs/ECBs would indicate improvement in the Indian financial markets. On the other hand, if the market for Indian GDRs remains good and yet FIIs shy from investing directly in the Indian markets then it could be an indication of problems in investing on the Indian markets.

The strategic objective does not speak of the development of the foreign exchange market (e.g.. The forex clearing house and the futures exchange). However, ultimately the Indian markets can be linked to the global markets only through the forex markets and this would become important once full convertibility is achieved.
Since there is little forex activity as of now it may not make sense to benchmark it until the later stages of the FIRE project.

Strategic objective 1.3: Increased amount of private capital used to finance commercially viable urban environmental infrastructure

Data sources used: Project reports, Sector Assessment and Annual Evaluation from RHUDO, NIUA, IL&FS and HUDCO

Comments: This falls outside the purview of FIRE (PW-OGS) there is

Project outcome 1.11: Clearing and settling time of traded securities are reduced in securities markets

Data Sources: Project reports of SEBI/NSE/FIRE/PW Contractor and SEBI reports.

Other sources: Stock exchanges and market participants

Comments: **The target depends to a large extent on the proposed depository and if this is set up then we would have a delivery versus payment system and hence the settling time would be reduced to much lesser than the 7-14 days targeted. Otherwise, this target seems difficult for the equity markets specially for the non-specified scrips.** The debt market (for government securities) already settles faster than indicated. The NSE debt trades work on a t+n system of settlement up to n = 5/6. In the case of the telephone market it is a delivery vs. payment system. This improvement, however, has happened only recently and if we benchmark at 1994-95 then the settlement period was longer.

Project outcome 1.12: Price transparency improved in securities markets (number of stock exchanges and trading volumes using the new system).

Data sources: Project reports of SEBI/NSE/PW Contractor and SEBI reports

Other sources: Stock exchanges and market participants

Comments: None

Project outcome 1.13: Increased number of financial instruments traded on stock exchanges

Data sources: Project reports of SEBI/NSE/PW Contractor and SEBI reports

Other sources: The futures exchange - whenever it is set up

Comments: **If the futures' exchange is set up then derivatives should be included in the baseline as PW-FIRE has done some work in terms of seminars etc. and also plans to do some in the direction of training.**
Also, the target of having **asset securitisation is again a function of macroeconomic factors.** If there is no term money market ther

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it will be difficult to benchmark a rate for the securitised assets. E.g., in the U.S., mortgages trade X basis points over the treasury rate. **Thus, this target should be subject to the development of a term money market.**

Project outcome 1.14:	Reduced amount of time it takes to list on the stock exchange after the initial public offering
Data sources:	Project reports of SEBI/NSE/PW Contractor and SEBI reports
Other sources:	None
Comments:	None

Project outcome 1.15:	Securities depository system established and functioning
Data sources:	Project reports of SEBI/NSE/PW Contractor and SEBI reports
Other sources:	None
Comments:	None

Project outcome 1.15:	Increased number of local and municipal governments involved in issuing financial instruments
Data sources:	Project reports of SEBI/NSE/PW Contractor and SEBI reports
Other sources:	None
Comments:	Outside the purview of PW-FIRE

Project outcome 1.21:	Increased number of issuers in the capital markets
Data sources:	Project reports of SEBI/NSE/PW Contractor and SEBI reports
Other sources:	None
Comments:	None

Project outcome 1.22:	Increased number of investors in the capital markets
Data sources:	Project reports of SEBI/NSE/PW Contractor and SEBI reports
Other sources:	Stock exchanges
Comments:	None

Project outcome 1.23:	Increased amount of private capital raised by small enterprises
Data sources:	OTCEI Annual report
Other sources:	BSE, CMIE, Prime Database, Capline, IDSS
Comments:	OTCEI allows listing of companies with capital, at the time of listing, between 30 lakhs to 25 crores. Now, BSE lists all companies that have a capital of more than 5 crores and NSE those greater than 10 crores. Thus, there is obviously an overlap and hence small issuers on BSE and the NSE should also be included. Besides this, the ratio of the private capital generated by small enterprises on the OTCEI vs. the NSE and the BSE should also be monitored to evaluate the progress made by OTCEI itself as, after all, the quality of issues on OTCEI is better as it has greater transparency. Capital raised by small enterprises in the recent past has been disproportionately high for finance companies. Now, such issues are suspect and hence if there is a decrease in the ratio of capital raised by finance companies as compared to the other sectors it is an indication of better regulation and transparency. Private capital raised by small enterprises is again dependent on the liquidity in the markets (a function of macroeconomic factors) and hence the absolute amount of capital raised by way of such issues may not be a good indicator. A possible solution is to

monitor the ratio of the capital raised by small enterprises against the total loan disbursements of the banking system and financial institutions. This is a proxy measurement and has the inherent assumption that the proportion of loan disbursements to smaller enterprises as compared to larger corporations will remain the same over the period being monitored, i.e., the duration of the FIRE project.

Project outcome 1.24: Increased percentage of household financial assets held in shares and debentures

Data sources: RBI estimates

Other sources: None

Comments: None, except that **there should be a similar project outcome in terms of an increase in the ratio of household financial assets as compared to physical assets.**

Appendix H

Biodata for Allan Roth and Russell Diehl

Mr. Allan Roth, Capital Markets Regulations Specialist & Senior Law Professor

Mr. Allan Roth has been a Senior Professor at Rutgers Law School since 1969, where he teaches courses in legal aspects of transnational business, managerial aspects of corporation law and securities regulation. Throughout this time period, Mr. Roth has engaged in consultancy services for financial institution development in a wide range of countries, in South America, Asia, the Middle East and Europe.. Consulting responsibilities have included participating in the formulation of development plans, preparing laws and regulations and providing technical assistance to government ministries/agencies, stock exchanges and nonbank financial institutions. Mr. Roth is also a noted publisher, his works vary from contributions to law reviews and books, to financial/capital market reports to foreign governments and businesses. Prior to his academic career and consultancy work, Mr. Roth was the Director for Legal and Government Affairs for the American Stock Exchange in New York, a member of the Staff of the General Counsel for the Securities Exchange Commission in Washington and in the private practive of law. Mr. Roth received his law degree from Harvard Law School.

Mr. Russell Diehl, Senior Investment Banking/Capital Markets Professional

Mr. Russell Diehl currently serves as the Managing Director for The duPont Reserve Corporation, where he has directed the development of over 500 underwriting, private placement and principal investment transactions for emerging and mid-sized clients. His consultancy work includes USAID projects in emerging and transition economies in India, Sri Lanka and Jordan. He has also been worked extensively in private and public sector commercial banking in Latin America. Prior to his work at The duPont Reserve Corp., Mr. Diehl was Vice President for the Union Bank of Los Angeles and an International Officer for The Bank of New York. Mr. Diehl holds an M.Sc. in International Business from the American Graduate School for International Management, Arizona and a B.A. in Economics.